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TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1932

No. 476

D. B. HEINER, COLLECTOR OF INTERNAL REVENUE FOR THE TWENTY-THIRD DISTRICT OF PENNSYLVANIA, PETITIONER

vs.

DIAMOND ALKALI COMPANY

No. 477

D. B. HEINER, COLLECTOR OF INTERNAL REVENUE FOR THE TWENTY-THIRD DISTRICT OF PENNSYLVANIA, PETITIONER

vs.

DIAMOND ALKALI COMPANY

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

PETITION FOR CERTIORARI FILED OCTOBER 26, 1932
CERTIORARI GRANTED DECEMBER 5, 1932

(37173)
(37174)

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1a **In United States District Court, Western District of Pennsylvania**

Docket entries

Aug. 25, 1928, præcipe for summons filed. Statement of claim filed. Summons issued.

Aug. 27, 1928, summons returned served on D. B. Heiner at Pittsburgh on Aug. 27, 1928.

Aug. 30, 1928, affidavit of service of statement of claim filed.

Sept. 21, 1928, præcipe for appearance of John D. Meyer and John A. McCann for defendant filed.

Nov. 7, 1928, affidavit of defense filed.

Dec. 20, 1928, on petition of John D. Meyer, rule granted on plaintiff to show cause why its books should not be examined by representatives of the defendant, rule returnable Jan. 2, 1929.

Dec. 28, 1928, plaintiff's answer to rule filed.

Jan. 14, 1929, plaintiff's reply to the new matter in defendant's affidavit of defense filed.

Jan. 15, 1929, on motion of plaintiff, amendments to statement of claim filed, by leave of court. Hearing on preliminary matters.

Jan. 18, 1929, on petition of plaintiff, order entered directing a subpœna duces tecum issue to T. Raymond Evans, president of defendant company.

2a Jan. 21, 1929, plaintiff's reply to affidavit of defense to plaintiff's amendments to its statement of claim filed. Defendant's affidavit of defense to amendment to statement of claim filed. Stipulation waiving jury trial filed. Trial opens before Gibson, J., without a jury. Subpœna duces tecum returned served on T. Raymond Evans on Jan. 19, 1929.

Jan. 22, 1929, trial continues.

Jan. 23, 1929, trial continues. Motion for judgment for plaintiff filed. Motion for judgment for defendant filed.

Jan. 24, 1929, trial closed. Trial memo filed at No. 5761 Law.

Feb. 5, 1929, transcript of testimony filed at No. 5761 Law.

Feb. 23, 1929, plaintiff's requests for findings of fact filed.

Feb. 26, 1929, defendant's request for findings of fact filed.

Feb. 10, 1930, opinion and order filed and entered directing that judgment be entered for the plaintiff and against the defendant in the sum of $198,954.59. Pursuant to the above order, judgment is hereby entered for the plaintiff, Diamond Alkali Company,

3a and against the defendant D. B. Heiner, collector of internal revenue, in the sum of $198,954.59.

J. Wood Clark, *Clerk.*

Feb. 14, 1930, on motion of both parties, order entered vacating the above judgment entered on Feb. 10, 1930, and directing that judgment be entered for the plaintiff and against the defendant in

the amount of $175,410.60, with interest from Nov. 15, 1927; exception reserved to plaintiff and bill sealed; exception reserved to defendant and bill sealed.

Feb. 14, 1930, pursuant to the above order, judgment is hereby entered for the plaintiff, Diamond Alkali Company and against the defendant D. B. Heiner, collector of internal revenue, in the amount of $175,410.60, with interest from Nov. 15, 1927.

J. Wood Clark, *Clerk.*

Apr. 23, 1930, certificate of probable cause filed. On petition of plaintiff, order entered allowing an appeal. Bill of exceptions filed, and order entered allowing and sealing same (original papers). Assignments of error filed. Plaintiff's appeal bond for costs approved by the court and filed.

Apr. 24, 1930, citation issued, returnable May 24, 1930.

4a May 13, 1930, on petition of D. B. Heiner, order entered allowing appeal. Assignments of error filed. Order of court filed and entered allowing defendant until May 28, 1930 to file bill of exceptions.

May 22, 1930, stipulation for printing record filed.

May 27, 1930, on stipulation, order entered allowing the plaintiff's bill of exceptions to be regarded as the defendant's bill of exceptions. Stipulation for printing defendant's appeal record filed.

In United States District Court

Statement of claim

Filed Aug. 25, 1928

Diamond Alkali Company, the above named plaintiff, has a claim against D. B. Heiner, collector of internal revenue for the twenty-third district of Pennsylvania, defendant, for the sum of $1,164,015.33, with interest thereon from November 15, 1927, upon a cause of action whereof the following is a statement:

I

1. Diamond Alkali Company, the plaintiff, is, and at all times herein mentioned was, a corporation organized and existing under the laws of the State of West Virginia, with its principal office in the city of Pittsburgh in the Commonwealth of Pennsylvania.

5a 2. D. B. Heiner, the defendant, is, and ever since on or about the first day of August, 1921, has been, the duly appointed, qualified, and acting collector of internal revenue for the twenty-third district of Pennsylvania, and now resides in the Borough of Kittanning and within said Western District.

3. For the years 1918 and 1920, the plaintiff kept its books of account on the accrual basis and filed its Federal income and profits tax returns on the accrual and calendar year basis.

4. On the 16th day of June, 1919, and on the 13th day of May, 1921, respectively, the plaintiff duly filed its said returns for the years 1918 and 1920 and then and thereafter duly paid to the defendant's predecessor in office as collector of internal revenue for the twenty-third district of Pennsylvania, and to the defendant as such collector, all taxes appearing by said returns to be due and owing to the Government of the United States, to wit, $1,074,749.11 for 1918, and $263,891.89 for 1920.

5. By letter dated July 11, 1927, the Commissioner of Internal Revenue (hereinafter called the "commissioner"), notified the plaintiff that its said returns were erroneous; that he, the commissioner, had made divers changes and adjustments in the plaintiff's tax liability and in the figures on which the same was computed; and that as the result of such changes and adjustments plaintiff owed to the Government of the United States, in addition to
6a the taxes previously paid as aforesaid, income and profits taxes of $1,215,615.14 (less credit of $1,467.64 for 1919 taxes overpaid) for 1918, and $60,769.03 for 1920, or the total sum of $1,274,916.53.

6. Pursuant to said letter, and on or about the first day of November, 1927, the commissioner, notwithstanding the plaintiff's protests, proceeded to assess against the plaintiff alleged additional income and profits taxes of $1,214,147.50 for 1918 and $60,769.03 for 1920.

7. On or about November 7, 1927, the defendant served upon the plaintiff written notice of said assessments and demand for payment of said alleged additional taxes, together with interest of $117,739.08 on said alleged tax of $1,214,147.50 for 1918, and interest of $5,892.93 on said alleged tax of $60,769.03 for 1920, or the total sum of $1,398,548.54; and defendant accompanied his demand with threats of penalties, further interest, and seizures of the plaintiff's property if payment should not be made within ten days.

8. Under duress and written protest, and for the sole purpose of avoiding the penalties, further interest, and seizures threatened by the defendant as aforesaid, the plaintiff paid said total sum of $1,398,548.54 to the defendant on or about the 15th day of November, 1927.

9. Said alleged additional tax for 1918 (except $188,387.39 thereof, which the plaintiff admits was owing) resulted from action by the commissioner as follows:

7a (a) Redetermination of plaintiff's allowance for the amortization of war-time facilities for the years 1918 and 1919 under section 234 (a) (8) of the revenue act of 1918 in the sum of $387,224.40 instead of permitting the same to stand at $1,344,465.15 as determined at the time and in the manner hereinafter described; whereby the plaintiff's deduction from 1918 gross income on account of said allowance was changed from $1,245,448.21 to $315,956.89.

(b) Disallowance of $439,104.16 of the total deduction, to wit, $876,366.71, taken by the plaintiff from gross income on its books and

on its returns for 1918 on account of wear, tear, exhaustion, and obsolescence of its depreciable physical assets.

(c) Determination of 54.54+% under section 328 of the revenue act of 1918 as the ratio of plaintiff's excess profits tax to its net income instead of 45% as demanded by the plaintiff.

11. Said above described adjustments by the commissioner were erroneous and illegal in all respects, and said alleged additional taxes and the assessment and collection thereof and of interest
8a thereon were and are erroneous, illegal, and void except to the extent of $188,387.39 of additional tax for 1918 (and interest thereon of $18,246.57) and $26,771.06 of additional tax for 1920 (and interest thereon of $2,595.48). Annexed hereto, marked "Exhibit 1" and made part hereof is a correct computation and statement of plaintiff's income and profits tax liability for 1918 and 1920, showing the amounts actually owing, the amounts that plaintiff was compelled to pay, and the amounts of alleged taxes and interest paid by the plaintiff in excess of the amounts owing and for the recovery of which this suit is brought.

II

12. At all times up to and including the third day of March, 1924, the amortization section of the Income Tax Unit and the employees thereof had full charge on the part of the commissioner of audit, investigation, and consideration of claims by taxpayers under section 234 (a) (8) of the revenue act of 1918 and section 234 (a) (8) of the revenue act of 1921 for allowances on account of amortization of war time facilities, and at all such times the chief or acting chief of said section had full power and authority from the commissioner, as plaintiff avers on information and belief, to determine the amounts of such allowances and give notice of such determinations to the claimants, and as matter of regular routine and practice did made such determinations and give such notices with full knowledge,
9a acquiescence, and approval on the part of the commissioner and without consideration or action by the commissioner personally.

13. Plaintiff constructed, erected, installed, and acquired, on or after April 6, 1917, certain buildings, machinery, equipment, and other facilities for the production of articles contributing to the prosecution of the war with Germany, and at the time of filing its said return for 1918 plaintiff duly made claim for deduction from gross income under section 234 (a) (8) of the revenue act of 1918 on account of amortization of war-time facilities, which claim was subsequently revised by the plaintiff, and the revised claim for $1,756,453.64 filed with the commissioner on or about September 10, 1921. Said sum of $1,756,453.64 was and is the correct amortization allowance to which the plaintiff was as a matter of fact entitled, and $1,487,001.78 thereof was deductible from plaintiff's gross income for 1918.

14. In the month of September, 1921, the commissioner, acting by the authorized officials of said amortization section, sent his representative, one F. R. Griffith, an engineer in said amortization section, to the plaintiff's properties with written instructions and authority to examine the same, investigate the facts and matters set out in the plaintiff's said revised claim, audit said claim in the light of such investigation, and submit a report and determination of the plaintiff's allowance under section 234 (a) (8) of the revenue act of 1918 to said amortization section.

10a 15. Said Griffith carried out his said instructions and on or about October 23, 1921, made a detailed written report to said amortization section covering his said examination, investigation, and audit and his findings of fact in the course thereof, and containing a determination that the plaintiff was entitled to an allowance under said section 234 (a) (8) in the sum, as plaintiff avers on information and belief, of $1,344,465.15, of which $1,245,448.21 should be deducted from 1918 gross income and $99,016.94 from 1919 gross income.

16. In the ordinary and usual course of business of the Income Tax Unit and said amortization section thereof, said report and determination came on for review before one B. L. Wheeler, chief of engineers in said amortization section and duly authorized by the commissioner in that behalf, and upon such review and consideration thereof the said B. L. Wheeler approved said report and determination in all respects, and on or about December 1, 1921, signified his approval in writing endorsed on said report.

17. On or about the first day of December, 1921, and in the ordinary and usual course of business of the Income Tax Unit and said amortization section, said report and determination came for final action before one T. J. S. Kishpaugh, acting chief of said amortization section, and, as plaintiff avers on information and belief, authorized by the commissioner to take such final action and to make determination of the plaintiff's allowance with the same effect

11a as if by the commissioner personally, and said Kishpaugh then and there approved said report and determination and signified his approval by endorsement in writing on said report.

18. On or about the 10th day of January, 1922, a copy of said report and determination, with said endorsements thereon, was delivered to the plaintiff by said amortization section on behalf of and with the authority of the commissioner and, notwithstanding that the correct allowance was $1,756,453.64 as aforesaid, was nevertheless accepted by the plaintiff without further objection.

19. The plaintiff never thereafter requested a reexamination of its returns with respect to said allowance. The commissioner did not thereafter at any time before March 3, 1924, reexamine said return with respect to said allowance, or determine that said allowance of $1,344,465.15 was erroneous, or make or begin or cause to be made or begun any new investigation or reexamination of said allowance, or make any appraisal, or obtain any other evidence, or take any further action or do any other thing whatsoever in respect

to said allowance. On the contrary, plaintiff avers on information and belief that from the time of said approval of said determination of $1,344,465.15 by said acting chief of section as above described to on or about October 1, 1924, no further proceedings were had or taken with respect to plaintiff's amortization allowance, the same having been finally and definitely determined as hereinbefore averred.

12a 20. On or about October 1, 1924, some person in said amortization section unknown to the plaintiff assigned the matter of said allowance for reexamination. No reexamination or reinvestigation was made or begun, however, until on or about April 1, 1925, when one Luce, an engineer in said amortization section, made an investigation and examination of plaintiffs' properties; and on or about November 4, 1925, said Luce made a report to said amortization section covering his investigation and examination, and containing an alleged determination of plaintiff's said allowance at $468,812.30. On or about November 4, 1925, said amortization section sent to the plaintiff a copy of said report and determination entitled "Redetermination of taxpayers' claim for amortization."

21. On or about November 17, 1926, the plaintiff received from said amortization section a paper entitled "Second redetermination of amortization claim," wherein the plaintiff's said allowance was alleged to be determined at $387,224.40, of which $369,022.30 was apportioned to 1918 and $18,202.10 to 1919.

22. Said alleged "Second redetermination" was used by the commissioner in computing the plaintiff's net income for 1918 and assessing against the plaintiff said alleged additional tax for that year.

23. Plaintiff is advised by counsel and therefore avers that it was and is lawfully entitled to said allowance in the sum of $1,344,465.15 regularly and finally determined as above described, and to

13a deduction of $1,245,448.21 from its 1918 gross income, and that said two subsequent alleged redeterminations under the circumstances above set forth and being subsequent to March 3, 1924, were and are in violation of section 234 (a) (8) of the revenue act of 1921, and of no legal effect whatsoever, and plaintiff further avers that the said alleged redeterminations were not based upon any new and material evidence or any mathematical error or mistake or the discovery of any fraud in the original determination theretofore made.

III

24. During the year 1918 the plaintiff actually sustained wear, tear, exhaustion, and obsolescence of its depreciable physical assets in the sum of $876,366.71, and duly deducted said sum of $876,366.71 from gross income upon its books of account and its said return for 1918.

25. Nevertheless the commissioner disallowed for 1918 $439,104.16 of said deduction of $876,366.71 and allowed only $437,262.55 thereof.

26. To the extent that the commissioner disallowed the plaintiff's deductions for wear, tear, exhaustion, and obsolescence of depreciable physical assets as aforesaid, his action deprived the plaintiff of the deductions from gross income to which it was entitled and of wear, tear, exhaustion, and obsolescence of depreciable physical assets actually sustained by the plaintiff, and was erroneous, illegal, and void.

14a

IV

27. On application by the plaintiff the commissioner found and so declared of record that the plaintiff's excess profits tax of 1918, if determined without the benefit of section 327 of the revenues act of 1918, would, owing to abnormal conditions affecting the capital or income of the plaintiff, work upon the plaintiff an exceptional hardship evidenced by gross disproportion between the tax computed without the benefit of said section 327 and the tax computed by reference to the representative corporations specified in section 328 of the revenue act of 1918.

28. In computing the plaintiff's excess profits tax for 1918 under said section 328, the commissioner determined the ratio of tax to net income at 54.54+%, arriving at that ratio, as he claimed, on the basis of the ratio of average tax to average net income (in excess of the specific exemption of $3,000) of representative corporations engaged in a like or similar trade or business to that of the plaintiff.

29. The plaintiff does not know, and has been unable to ascertain from the commissioner, what specific corporations the commissioner used as comparatives under said section 328, but avers on information and belief that the same were not, as required by said section 328, representative corporations engaged in a like or similar trade or business to that of this plaintiff.

15a 30. During 1918 and several years prior and subsequent thereto, the following corporations were engaged in a like or similar trade or business to that of the plaintiff and were the only persons or corporations in the United States engaged in such like or similar trade or business: Michigan Alkali Company, of Detroit, Michigan; Matheson Alkali Works, of New York City; Columbia Chemical Company, of Pittsburgh, Pennsylvania; Solvay Process Company, of Solvay, New York.

31. Plaintiff avers on information and belief that for the year 1918 the ratio of the average tax of representative corporations engaged in a like or similar trade or business to that of the plaintiff to their average net income (in excess of the specific exemption of $3,000) was not in excess of 45%.

32. The plaintiff avers on information and belief that the commissioner's determination of the ratio of plaintiff's excess profits tax for 1918 to its net income for that year (in excess of the specific exemption of $3,000) at 54.54+% was erroneous, illegal, and void, that the correct ratio was 45%, and that said ratio of 45% ought

to have been used by the commissioner under said section 328.

16a [Omitted.]

17a VI

40. Except for $188,387.39 (and interest thereon of $18,246.32) for 1918 and $26,771.06 (and interest thereon of $2,595.48) for 1920, the said alleged additional taxes for 1918 and 1920 and the interest thereon paid by the plaintiff as hereinabove stated, and the assessment and collection thereof, were in all respects erroneous, illegal, and void.

41. On or about the 23rd day of December, 1927, the plaintiff filed with the commissioner, on the forms prescribed by him for that purpose, claims for refund of said overpayments of taxes (and interest) for 1918 and 1920, on the grounds that the said taxes as overpaid and the assessment and collection thereof were in all respects erroneous, illegal, and void; but on or about the 13th day of April, 1928, said claims and each of them were wholly rejected by the commissioner.

42. No part of said overpayment of taxes and interest has been repaid or refunded to the plaintiff, and the defendant is indebted to the plaintiff as follows:

18a

Year	Tax overpaid	Interest overpaid
1918	$1,027,227.75	$99,492.76
1920	33,997.37	3,297.45

Wherefore, this suit is brought and plaintiff claims judgment against the defendant for the sum of $1,164,015.33 with interest thereon from November 15, 1927.

SMITH, SHAW & MCCLAY,
Attorneys for Plaintiff.

[*Duly sworn to by W. E. Jones; jurat omitted in printing.*]

19a *Exhibit 1 to statement of claim*

1918

Net income		$2,452,548.15
Excess profits tax at 45% of the net income		1,103,646.66
Income tax:		
Net income	$2,452,548.15	
Less exemption:		
Liberty bond interest	17,819.46	
Excess profits tax	1,103,646.66	
Specific exemption	2,000.00	
Net income	$1,329,082.03 @ 12%	159,489.84
Total correct tax		$1,263,136.50

1918

Tax payments:		
With return	$1,074,749.11	
Nov. 15, 1927	1,215,615.14	
Total tax paid		2,290,364.25
Tax overpaid		$1,027,227.75
Interest on tax overpaid		99,492.76
Tax and interest overpaid		$1,126,720.51
Interest paid Nov. 15, 1927 on $1,215,615.14	$117,739.08	
Interest on the correct deficiency of $188,387.39 @ .09685	18,246.57	
Interest overpaid	$99,492.51	

20a

1920

Net income		$1,529,710.37
Invested capital		8,950,735.25
Excess profits tax credit		719,058.82
Excess profits tax		162,130.31
Income tax:		
Income	$1,529,710.37	
Less exemptions:		
Liberty bond interest	$80,253.71	
Excess profits tax	162,130.31	
Specific exemption	2,000.00	244,384.02
Taxable @ 10%	$1,285,326.35	128,532.64
Correct tax liability		$290,662.95
Tax payments:		
With return	$263,891.89	
Paid 11/15/27	60,769.03	
Total amount paid		324,660.92
Tax overpaid		33,997.97
Interest on tax overpaid		3,297.45
Tax and interest overpaid		$37,295.42
Interest paid 11/15/27 on $60,769.03	=$5,892.93	
Interest on correct defficiency of $26,771.06 @ .096972	= 2,595.48	
Interest overpaid	$3,297.45	

21a

In United States District Court

Affidavit of defense

Filed Nov. 7, 1928

Comes now D. B. Heiner, defendant above named: alleges that he has a full, just, true, and legal defense to all of the plaintiff's statement of claim: and says that the nature of the defense is as follows:

I

1. Defendant admits the allegations contained in paragraph 1 of the statement of claim.

2. Defendant admits the allegations contained in paragraph 2 of the statement of claim.

3. Defendant admits the allegations contained in paragraph 3 of the statement of claim.

4. Defendant admits the allegations contained in paragraph 4 of the statement of claim.

5. Defendant admits the allegations contained in paragraph 5 of the statement of claim.

6. Defendant admits the allegations contained in paragraph 6 of the statement of claim.

7. Defendant admits the allegations contained in paragraph 7 of the statement of claim.

8. Defendant admits the allegations contained in para-
22a graph 8 of the statement of claim, except that the said payment was made under duress. Defendant alleges that said payment was not accompanied by duress of any kind.

9. In answer to the allegations contained in paragraph 9 of the statement of claim, defendant admits that the alleged additional tax for 1918, except $188,287.39 thereof, which plaintiff admits was owing, resulted from the action of the commissioner in—

(a) Determining plaintiff's allowance for amortization of wartime facilities for the years 1918 and 1919 under section 234 (a) (8) of the revenue act of 1918, in the sum of $387,224.40, instead of permitting the same to stand at $1,344,465.15, whereby plaintiff's deduction from 1918 gross income on account of said allowance was changed from $1,245,448.21 to $315,956.89;

(b) The disallowance of $439,104.16 of the total deduction of $876,366.71 taken by plaintiff from gross income on its books and on its returns for 1918 on account of wear, tear, exhaustion, and obsolescence of its depreciable physical assets; and

(c) The determination of 54.54% under section 328 of the revenue act of 1918 as the ratio of plaintiff's excess-profits tax to its net income, instead of 45% as demanded by the plaintiff.

Defendant denies that plaintiff's said allowance for amorti-
23a zation was ever determined in the sum of $1,344,465.15, and alleges that the said allowance was correctly determined in the amount of $387,224.40 and that plaintiff's correct allowance for the year 1918 as a deduction from its gross income for said year on account thereof, was $315,956.89. Defendant denies that $876,366.71 represents the true and correct deduction allowable to plaintiff because of wear, tear, exhaustion, and obsolescence of its depreciable physical assets, and on the contrary, alleges that the Commissioner of Internal Revenue properly disallowed $439,104.16 of the total deduction claimed.

Defendant further alleges that this court is without jurisdiction to review the action of the Commissioner of Internal Revenue in computing and determining plaintiff's excess profits taxes for said years, or either of them, under sections 327 and 328 of the revenue

act of 1918, and is without jurisdiction to recompute or to determine at all plaintiff's excess profits tax at 54.54%, or any percentage of its income or revised income for the year 1918 under said sections 327 and 328 of the revenue act of 1918.

24a 11. In answer to the allegations contained in paragraph 11 of the statement of claim, defendant denies that the said adjustments by the commissioner were erroneous, illegal, or void, and alleges that each of them was in all respects correct, legal, and valid. Defendant denies that said additional taxes and the assessment and collection thereof, including interest, were erroneous, illegal or void (except to the extent of $188,387.39 of the additional tax for 1918, with interest thereon of $18.246.57 and $26.771.06 of the additional tax for 1920, with interest thereon of $2,595.48). On the contrary, defendant alleges that the assessment and the collection thereof were each legal, correct, and valid. Defendant denies that Exhibit I, attached to the statement of claim and made a part thereof, is a correct computation or statement of plaintiff's income or profits tax liability for 1918 and 1920, or either of them, and denies that it shows the amounts actually owing or amounts actually paid in excess of amounts owing either in tax or interest. On the contrary, defendant alleges that plaintiff's income and excess profits taxes for the years 1918 and 1920, respectively, were determined and lawfully assessed against the plaintiff, and collected from it, in the following respective amounts: $2,290,364.25 for 1918 and $324,660.92 for 1920; and that a true and correct computation and statement of plaintiff's in-

25a come and profits tax liability for the years 1918 and 1920 is attached hereto, made a part hereof, and marked "Exhibit I," reference to which is hereby made.

II

12. In answer to the allegations contained in paragraph 12 of the statement of claim, defendant denies that at all times up to and including March 3, 1924, the amortization section of the Income Tax Unit, and/or the employees thereof, had full charge on the part of the commissioner or otherwise, of the audit, investigation, and consideration of claims by taxpayers under section 234 (a) (8) of the revenue act of 1918 or section 234 (a) (8) of the revenue act of 1921, for allowance on account of amortization of war-time facilities. On the contrary, defendant alleges that the function of said amortization section was at all times only to make investigations, examinations, and recommendations as to the allowance of said claims, and that said recommendations were subject to further audit and review by the Bureau of Internal Revenue. Defendant further denies that at all such times the chief and/or acting chief of said section had any power or authority from the commissioner to determine the amount of such allowances or to give notices of such determinations to claimants; and denies that as a matter of regu-

lar routine and practice the said chief or acting chief did make such determinations or give such notices with any knowledge, acquiescence, or approval on the part of the commissioner, or
26a without consideration or action by the commissioner personally. On the contrary, defendant alleges that the said chief and/or acting chief of said section had no power or authority to determine the amount of such allowances; that the power or authority to determine the allowable deduction from gross income on account of allowances under said sections of the said revenue acts, was and is, vested in the Commissioner of Internal Revenue; that the report and recommendation of said amortization section was subject to audit and review by the various audit and review sections of the Bureau of Internal Revenue; and that before allowance was or could be made or become final, and before it was or could be a determination or redetermination thereof within the meaning of the said sections of the said revenue acts, such allowance was subject to the approval of the commissioner, personally, or the assistant to the Commissioner of Internal Revenue. Defendant admits that as a matter of regular routine and practice, notice of the report and recommendation of the amortization section was delivered to the plaintiff.

13. In answer to the allegations contained in paragraph 13 of the statement of claim, defendant admits that plaintiff constructed, erected, installed, and acquired, on or after April 6, 1917, certain buildings, machinery, equipment, and other facilities for the production of articles contributing to the prosecution of the war with Germany, and at the time of filing its said return for 1918 plaintiff duly made claim for deduction from gross income under section 234 (a) (8) of the revenue act of 1918 on account of amorti-
27a zation of war-time facilities, which claim was subsequently revised by the plaintiff, and the revised claim for $1,756,453.64 filed with the commissioner on or about September 10, 1921.

Defendant denies that said sum of $1,756,453.64 was, or is, the correct amortization allowance to which plaintiff was, or is, as a matter of fact, entitled; and denies that $487,001.78 thereof was deductible from plaintiff's gross income for 1918. On the contrary, defendant alleges that the correct amount of plaintiff's amortization allowance was $387,224.40, of which amount $315,956.89 was deductible from plaintiff's gross income for 1918.

14. Defendant admits the allegations contained in paragraph 14 of the statement of claim, except that defendant denies that said F. R. Griffith was authorized or directed to determine the amount of plaintiff's amortization allowance under section 234 (a) (8) of the revenue act of 1918. On the contrary, defendant alleges that the sole power of said Griffith was to investigate and report on the said subject.

15. In answer to the allegations contained in paragraph 15 of the statement of claim, defendant admits that said Griffith carried out

his instructions and, on or about October 23, 1921, made a detailed written report to said amortization section, covering his investigation and audit. Defendant denies, however, that the said Griffith determined plaintiff's amortization allowance in any sum; and
28a denies that said report constituted a determination that plaintiff was entitled to any allowance under the said section 234 (a) (8) of the revenue act of 1918. On the contrary, defendant alleges that said report was merely a recommendation of said Griffith that plaintiff be allowed an amortization deduction in the amount of $1,344,465.15, of which amount $1,245,448.21 was deductible from 1918 gross income.

16. In answer to the allegations contained in paragraph 16 of the statement of claim, defendant admits that in the ordinary and usual course of business of the Income Tax Unit, said report came for review before one B. L. Wheeler, chief of engineers, in said amortization section; and admits that, upon such review and consideration thereof, the said B. L. Wheeler approved said report and, on or about December 1, 1921, signified his approval in written endorsement thereon. Defendant denies that said B. L. Wheeler and/or said Griffith determined or were authorized to determine plaintiff's amortization allowance in any sum whatsoever; denies that said report constituted a determination of plaintiff's amortization allowance; denies that any determination came on for review before said B. L. Wheeler; and denies that said B. L. Wheeler approved any determination thereof. On the contrary, defendant alleges said report was a mere recommendation which was approved by said B. L. Wheeler.

17. In answer to the allegations contained in paragraph 17
29a of the statement of claim, defendant admits that on or about the first day of December, 1921, in the ordinary and usual course of business of the Income Tax Unit said report came on for review and action before one T. J. S. Kishpaugh, acting chief of said amortization section, and that said Kishpaugh then and there approved said report and signified his approval in written endorsement thereon. Defendant denies that said report constituted a determination of plaintiff's amortization allowance; denies that said report and/or any determination of plaintiff's amortization allowance came for final action before said Kishpaugh; denies that said Kishpaugh had any authority or power to make any determination or to take any final action relative to plaintiff's allowance with the same effect as if made by the Commissioner of Internal Revenue personally. On the contrary, defendant alleges: that said report constituted a mere recommendation relative to the amount of amortization allowance deductible by the plaintiff; that the action of said Kishpaugh was merely a concurrence in the recommendation thus previously made; that said Kishpaugh had no power or authority on behalf of the Commissioner of Internal Revenue to take any

final action relative to plaintiff's amortization allowance or to determine it; and that the action of said Kishpaugh was subject to further audit and review in the Bureau of Internal Revenue as herein above set forth.

18. In answer to the allegations contained in paragraph 18 of the statement of claim, defendant admits that a copy of said report was delivered to plaintiff by said amortization section under
30a authority from the Commissioner of Internal Revenue. Defendant alleges that said copy was delivered on or about December 2, 1921, and not on or about the tenth day of January, 1922, as alleged in said paragraph. Defendant denies that the correct deduction allowable to plaintiff on account of amortization was $1,756,453.64, and alleges that the correct deduction allowable to plaintiff was $387,224.40. Defendant further alleges that said deduction allowed to plaintiff was fair, reasonable, and correct. Defendant denies that said report was accepted by the plaintiff without further objection. To the contrary, defendant alleges that plaintiff, on several occasions, expressed a willingness to accept it, provided plaintiff's "case" could then and thereupon be closed.

Defendant further alleges that said report (as appears on the face thereof) was but a recommendation relative to said amortization claims; that the report was subject to further audit; and that, at the time said report was delivered to the plaintiff, plaintiff was advised that said report was subject to review and was only a recommendation relative to the matters therein contained.

19. In answer to the allegations contained in paragraph 19 of the statement of claim, defendant denies that plaintiff never thereafter requested a further examination of its said returns with respect to said allowance. On the contrary, defendant alleges that plaintiff, thereafter, in briefs filed by it, requested the commissioner
31a to make further adjustments in its said amortization allowance. Defendant admits that the commissioner did not thereafter, at any time prior to March 3, 1924, commence a reexamination of said returns with respect to said allowance, but defendant alleges that the first reexamination of said return with respect to said allowance was begun in the year 1921 and had not been completed on March 3, 1924, and was not completed until several years thereafter. Defendant denies that the commissioner did not determine that said allowance of $1,344,465.15 was erroneous and alleges that said amortization allowance was never determined at such sum. Defendant denies that the commissioner did not, subsequent to March 3, 1924, make further investigations and examinations and take further action with respect to plaintiff's amortization allowance. To the contrary, defendant alleges that plaintiff's said returns and plaintiff's claim for amortization allowance were continuously, from the year 1921 to a time long subsequent to March 3, 1924, in process of audit, investigation, and consideration. Defendant denies that no further proceedings were had or taken with respect to plaintiff's

amortization allowance after said Griffith's report and the recommendation therein contained had been approved by said acting chief of the amortization section in the amount of $1,344,465.15 on or about October 1, 1924. On the contrary, defendant alleges that said claim was continuously in process of audit as above set forth. Defendant further denies said report or its approval by said section officer constituted a determination and alleges that said allowance for amortization was not actually determined until it was ap-
32a proved and allowed by the assistant to the commissioner on, or about, July 11, 1927.

20. In answer to the allegations contained in paragraph 20 of the statement of claim, defendant admits that on or about October 1, 1924, some person in the amortization section assigned the matter of plaintiff's claim for further examination. Defendant denies that the claim was assigned for reexamination within the meaning of section 234 (a) (8) of the revenue act of 1918 or section 234 (a) (8) of the revenue act of 1921, and alleges that said further examination was a continuance of the audit theretofore begun. Defendant denies that no reexamination or reinvestigation was made, or begun, until on or about April 1, 1925, and alleges that the one and only reexamination and reinvestigation of plaintiff's return was commenced prior to March 3, 1924, and ended subsequently thereto. Defendant admits that one Luce, an engineer in said amortization section, made an investigation and examination of plaintiff's properties on or about April 1, 1925, and that on or about November 4, 1925, he made a report to said section covering his investigation and examination. Defendant denies said report was a determination of any kind and alleges that (as appears on the face thereof) it was a mere recommendation regarding plaintiff's said claim to the effect that it be determined at $468,812.30, and that said report was subject to further review. Defendant admits that, on or about November 4, 1925, said amortization section sent to the plaintiff a copy of said report entitled "Redetermination of taxpayer's claim for amortization."

33a 21. In answer to the allegations contained in paragraph 21 of the statement of claim, defendant admits that, on or about November 17, 1926, plaintiff received from said amortization section, a paper entitled "Second redetermination of amortization claim." Defendant denies that plaintiff's said allowance was alleged therein to be determined at $387,224.40 (of which $369,022.30 was apportioned to the year 1918 and $18,202.10 to the year 1919). On the contrary, defendant alleges said report constituted a mere recommendation, and showed, on its face, that it was subject to further review, and was not a determination of plaintiff's said amortization allowance in any sum whatsoever.

22. In answer to the allegations contained in paragraph 22 of the statement of claim, defendant admits that the Commissioner of Internal Revenue approved the recommendation contained in said

alleged second redetermination and used said report and recommendation in computing plaintiff's net income and tax liability for the year 1918. Defendant alleges that the total deduction allowable to plaintiff for 1918 on account of amortization was $315,956.89.

23. In answer to the allegations contained in paragraph 23 of the statement of claim, defendant denies that plaintiff is lawfully entitled to said amortization allowance in the sum of $1,344,465.15; denies that said allowance was in any way determined or allowed at such an amount, and denies that plaintiff is entitled to a de-
34a duction of $1,245,448.21 thereof from its 1918 gross income. On the contrary, defendant alleges that such an allowance was determined at $387,224.40 and that of the latter amount plaintiff is entitled to a deduction of $315,956.89 from its gross income for the year 1918 and is entitled to no further amortization. Defendant denies that plaintiff's claim was determined or allowed, or redetermined, prior to the action of the assistant to the Commissioner of Internal Revenue on July 11, 1927. Defendant further denies that the said reports of the engineers of the amortization section, which were thereafter approved by the chief or acting chief of said amortization section, constituted determinations within the purview of section 234 (a) (8) of the revenue act of 1918. On the contrary, defendant alleges that the said reports were merely the recommendations of the subscribers thereto that plaintiff's said claim be allowed in the amounts stated in said reports, respectively. Defendant denies that the report and recommendation upon which the commissioner based his determination of the amount of plaintiff's amortization allowance was not based upon any new and material evidence or mathematical error or mistake. On the contrary, defendant alleges said report and the said determination were based on new and additional evidence; that said Griffith erred in the recommendation made by him in his report; that his report was based on the assumed fact that several plant units of plaintiff were no longer required by plaintiff in the operation of its business, whereas, in truth and in fact, said plant units were but temporarily idle and were required by plaintiff in the operation of its
35a business; that said investigation and report of F. R. Griffith was made during a period of temporary business depression and did not reflect the normal condition of plaintiff's business during the postwar period; that, upon field investigation subsequent to said Griffith's report, it was discovered that the cost upon which amortization had been recommended was greatly in excess of the true amount thereof.

III

24. In answer to the allegations contained in paragraph 24 of the statement of claim, defendant denies that, during the year 1918, the plaintiff actually sustained wear, tear, exhaustion and/or obsolescence of its depreciable assets in the sum of $876,366.71. On

the contrary, defendant alleges that the wear, tear, exhaustion, and obsolescence actually sustained by the plaintiff was not in excess of $437,262.55 in said year. Defendant admits that the defendant deducted said sum of $876,366.71 upon its books of account and in its return for the year 1918.

25. The allegations contained in paragraph 25 of the statement of claim are admitted.

26. In answer to the allegations contained in paragraph 26 of the statement of claim, defendant denies that to the extent that the commissioner disallowed the plaintiff's deductions for wear, tear, exhaustion and/or obsolescence of depreciable assets, his action deprived plaintiff of any deductions from gross income to which
36a it was entitled; and denies that said action of the commissioner was erroneous, illegal, or void. On the contrary defendant alleges that plaintiff was allowed a correct, just, and legal deduction for wear, tear, exhaustion and/or obsolescence of depreciable assets for said year; and further alleges that said action of the commissioner was in all respects lawful, just, fair, and reasonable.

IV

27. The allegations contained in paragraph 27 of the statement of claim are admitted.

28. The allegations contained in paragraph 28 of the statement of claim are admitted.

29. In answer to the allegations contained in paragraph 29 of the statement of claim, defendant denies that the corporations used by the commissioner as comparatives under section 328 of the revenue act of 1918 were not representative corporations engaged in a like or similar trade or business to that of the plaintiff. On the contrary, defendant alleges that the corporations used for comparative purposes by the Commissioner of Internal Revenue in arriving at plaintiff's tax under section 328 of the revenue act of 1918 were each a representative corporation engaged in a like or similar trade or business to that of the plaintiff; that they were corporations whose invested capital could be determined under section 326 of the revenue act of 1918; that they were corpora-
37a tions which were, as nearly as might be, similarly circumstanced to plaintiff with respect to gross income, net income, profits per unit of business transacted, and capital employed, amount and rate of war profits and excess profits, and all other relevant facts and circumstances.

30. In answer to the allegations contained in paragraph 30 of the statement of claim, defendant denies that the Michigan Alkali Company of Detroit, Michigan; the Matheson Alkali Works of New York City; the Columbia Chemical Company of Pittsburgh, Pennsylvania, and/or the Solvay Process Company of Solvay, New York, were the only corporations engaged in a like or similar trade or busi-

ness to that of the plaintiff. On the contrary, defendant alleges that the corporations used by the Commissioner of Internal Revenue in computing plaintiff's tax under section 328 of the revenue act of 1919 (as above stated), were engaged in a like and/or similar trade or business to that of the plaintiff in the year 1918. Defendant further alleges that said Michigan Alkali Company, Matheson Alkali Works, Columbia Chemical Company, and Solvay Process Company, were not corporations whose invested capital could be satisfactorily determined under section 326 of the revenue act of 1918 and were not as nearly as might be, similarly circumstanced to plaintiff with respect to gross income, net income, profits per unit of business and/or capital employed, and/or the amount and rate of war profits or excess profits and/or all other relevant facts and circumstances.

38a 31. In answer to the allegations contained in paragraph 31 of the statement of claim, defendant denies that, for the year 1918, the ratio of the average tax of representative corporations engaged in a like or similar trade or business to that of the plaintiff to their average net income (in excess of the specific exemption of $3,000) was not in excess of 45%. To the contrary, defendant alleges that said ratio of the average tax of representative corporations (engaged in a like and/or similar trade or business to that of the plaintiff) to their average net income (in excess of the specific exemption of $3,000) was 54.54+% as determined by the Commissioner of Internal Revenue pursuant to the provisions of section 328 of the revenue act of 1918.

32. In answer to the allegations contained in paragraph 32 of the statement of claim, defendant denies that the commissioner's determination of the ratio of plaintiff's excess profits tax for 1918 to its net income for that year (in excess of the specific exemption of $3,000) at 54.54+% was erroneous, illegal, or void. On the contrary, defendant alleges that said determination by the Commissioner of Internal Revenue was in all respects correct, legal, valid, and just. Defendant denies that the correct ratio was 45% and denies that said ratio of 45% should have been used by the commissioner under said section 328. On the contrary, defendant alleges that the ratio of 54.54+% actually used by the commissioner in making his said determination was in all respects correct and was the ratio which should have been, and was, used by the commissioner as aforesaid.

39a 33. In further answer to the allegations contained in paragraphs 27 to 32, inclusive, of the statement of claim, defendant alleges (with all due respect to this honorable court) that the action of the Commissioner of Internal Revenue in computing and determining plaintiff's excess profits tax liability, as aforesaid, under section 328 of the revenue act of 1918 was, and is, discretionary, confided entirely to the said commissioner by the Congress and not subject to judicial review in this or any other court. Defendant alleges that

this court is without jurisdiction to review the said determination (pursuant to said section 328) made by the Commissioner of Internal Revenue.

34. Defendant alleges, in further answer to the allegations contained in paragraphs 27 to 32, inclusive, of the statement of claim, that this court is without the power, authority, jurisdiction or facilities to compute plaintiff's excess profits taxes for the year 1918 under said remedial section 328 of the revenue act of 1918.

35. In further answer to the allegations contained in paragraphs 27 to 32, inclusive, of the statement of claim, defendant alleges that the allegations contained in said paragraphs do not state facts sufficient to constitute a cause of action against the defendant and do not state facts constituting any part of a cause of action against the defendant.

40a [Omitted.]

41a VI

40. In answer to the allegations contained in paragraph 40 of the statement of claim, defendant denies that, except for $188,387.39 (and interest thereon of $18,246.32) for 1918 and $26,771.06 (and interest thereon of $2,595.48) for 1920, the said alleged additional taxes for 1918 and 1920, and/or the interest thereon, paid by the plaintiff or the assessment or collection thereof were in any way erroneous, illegal or void. On the contrary, defendant alleges that the action of the Commissioner of Internal Revenue in assessing and collecting from the plaintiff the sums of $1,215,615.14 and $60,769.03 for the years 1918 and 1920, respectively, with interest thereon, was in all respects legal, correct and valid.

41. The allegations contained in paragraph 41 of the statement of claim are admitted.

42a 42. Defendant admits that no part of the taxes and interest thereon, hereinabove described, has been refunded to the plaintiff. Defendant denies, however, that he is indebted to the plaintiff in the sums of $1,027,227.75 (together with interest thereon of $99,492.76) for the year 1918 or of $33,997.37 (with interest thereon of $3,297.45) for the year 1920. On the contrary, defendant alleges that said taxes and interest were lawfully and correctly collected and defendant owes plaintiff nothing, and is not indebted to plaintiff.

FIRST SEPARATE DEFENSE

As a further and separate defense to the allegations contained in the statement of claim, defendant alleges that—

43. This court is without jurisdiction to review the action of the Commissioner of Internal Revenue in computing plaintiff's profits tax for 1918 under said sections 327 and 328 of the revenue act of 1918 at 54.54% (or any other percentage) of plaintiff's net income or revised net income.

44. The allegations contained in the statement of claim do not state facts sufficient to constitute a cause of action against the defendant.

SECOND SEPARATE DEFENSE

As a further, and second, separate defense to the allegations of the statement of claim, defendant alleges that—

43a 45. The allegations contained in the first separate defense are incorporated herein as if fully at this point set forth in detail.

46. The amount of excess profits tax due from the plaintiff for the years 1918 and 1919, respectively, was computed by the Commissioner of Internal Revenue under the relief provisions of sections 327 and 328; for the year 1918, plaintiff's excess profits tax was computed under said sections to be 54.54+% of its net income for the year; if the income and/or invested capital found by the said commissioner to be plaintiff's true income and invested capital for said year are in any way modified, then the amount of profits tax due from plaintiff for 1918 may not be computed by the court under said sections 327 and 328 in any event, but must be computed (if at all) under section 301 of the said revenue act of 1918.

47. If plaintiff's claims for an additional deduction on account of amortization and depreciation are allowed in any further sums whatsoever for the year 1918, then plaintiff's invested capital for the year 1920 must be recomputed and reduced accordingly. Depreciation is not allowable upon cost on which amortization is allowed, and if plaintiff's amortization allowance for 1918 is increased, its depreciation allowance will be decreased for said year.

48. If plaintiff's claim for an additional deduction from its gross income for 1918 on account of amortization of war-time facili-

44a ties and depreciation of its capital assets is allowed and plaintiff's profits tax is computed under section 301 of the revenue act of 1918, the adjustment resulting therefrom will greatly decrease the amount (if any) which could be recoverable in this action. A true and correct statement of plaintiff's gains, profits, income, and invested capital for the years 1918 and 1920, showing plaintiff's tax liability after its claims for additional deduction from its gross income for 1918 on account of amortization and depreciation shall have been allowed (if allowable at all) and its excess profits tax for 1918 shall have been computed under section 301 of the revenue act of 1918, is attached hereto, made a part hereof, and marked "Exhibit 2."

45a WHEREFORE, the defendant, having fully answered, demands that he have judgment in his favor, and that he go hence with his costs in this behalf expended.

D. B. HEINER,
Defendant.
JOHN D. MEYER,
United States Attorney for the Western District of Pennsylvania.
JOHN A. MCCANN,
Special Assistant to the U. S. Attorney,
Attorneys for the Defendant.

46a [*Duly sworn to by D. B. Heiner; jurat omitted in printing.*]

Exhibit 1 to affidavit

1918

Computation of the tax without giving effect to the statute of limitations and without reducing the excess profits rate employed by the commissioner.

Net income per letter of July 11, 1927			$3,821,143.63
Less:			
Correct depreciation		$876,336.71	
Depreciation allowed		437,262.55	
Additional depreciation		$439,104.16	
47a Correct amortization	$1,245,448.21		
Amortization allowed	315,956.89		
Additional amortization		$929,491.32	
Additional deductions			$1,368,595.48
Correct net income			$2,452,548.15
Excess profits tax at 54.54%			$1,337,619.76
Income tax:			
Net income		$2,452,548.15	
Less—			
Profits tax	$1,337,619.76		
Liberty bond interest	17,819.46		
Exemption	2,000.00		
		1,357,439.22	
Bal. taxable at 12%		$1,095,108.93	131,413.07
Total income and profits tax			$1,469,032.83
Tax payments:			
With return		$1,074,749.11	
Nov. 15, 1927		1,215,615.14	
Total payments		$2,290,364.25	
Deduct		1,469,032.83	
Tax overpaid		$821,331.42	
Interest overpaid		79,545.95	
Tax and interest overpaid		$900,877.37	

Interest paid Nov. 15, 1927, $117,739.08 or .09685 of $1,215,615.14.
Interest at .09685 on $821,331.42, $79,545.95.

48a 1920

Computation of the tax without giving effect to the statute of limitations.

Net income			$1,529,710.37
(On basis of commissioner's)			
Invested capital (rate of 54.54% tax for 1918)			8,744,838.92
Excess profits tax credit			702,587.11
Excess profits tax			165,424.65
Income tax:			
Net income		$1,529,710.37	
Less—			
Liberty bond interest	$80,253.71		
Profits tax	165,424.65		
Exemption	2,000.00		
		247,678.36	
Bal. taxable at 10%		$1,282,032.01	128,203.20
Total income and profits tax			$293,627.85
Tax payments:			
With return		$263,891.89	
Paid Nov. 15, 1927		60,769.03	
			324,660.92
Tax overpaid			$31,033.07
Interest overpaid			3,009.34
Tax and interest overpaid			$34,042.41

Interest paid Nov. 15, 1927, $5,892.93 or .096972 of $60,769.03.
Interest at 0.96972 on $31,033.07, $3,009.34.

49a *Exhibit 1*

1918

Net income as corrected			$3,821,143.63
Profits tax, section 328, 54.54% of net income			2,084,324.26
Net income		$3,821,143.63	
Less:			
Interest on United States obligations not exempt	$17,819.46		
Profits tax	2,084,324.26		
Exemption	2,000.00		
		2,104,143.72	
Balance taxable at 12%		$1,716,999.91	
Tax at 12%			206,039.99
Correct tax liability			$2,290,364.25

1920

Net income corrected			$1,529,710.37
Invested capital			$6,992,170.97
Plus:			
(a) Adjustment for 1918 tax liability			269,805.61
(b) Adjustment for 1919 tax liability			84,064.49
Adjusted invested capital			$7,346,041.07
(Under paragraph—of the affidavit of defense, it is admitted that plaintiff is entitled to a further addition of $304,920.97 to its invested capital as above adjusted)			304,920.97
Invested capital, as now corrected			$7,650,962.04

50a COMPUTATION OF TAX

8% of invested capital ($7,650,962.04)		$612,076.96
Exemption		3,000.00
Excess profits credit		$615,076.96
		Tax
Net income	$1,529,710.37	
Less excess profits credit	615,076.96	
Balance	$914,633.31	
Taxable at 20%	914,151.27	
Taxable at 40%	$482.04	$182,830.25
		192.82
Total profits tax		$183,023.07
Net income	$1,529,710.37	
Less:		
Interest on United States obligations not exempt	$80,253.71	
Excess profits tax	183,023.97	
Exemption	2,000.00	
	265,276.78	
Balance taxable at 10%	$1,264,433.59	126,443.36
Total tax due		$309,466.43

51a *Exhibit 2 to affidavit*

Computation of tax, if plaintiff's claim for an additional deduction on account of amortization and depreciation is allowed, and profits taxes are computed under section 301 of the 1918 revenue act

1918

NET INCOME

Net income as disclosed by office letter dated December 23, 1925		$3,821,143.63
Deduct:		
Depreciation claimed	$876,366.71	
Depreciation previously allowed	437,262.55	
Additional deduction	439,104.16	
Amortization claimed	$1,245,448.21	
Amortization previously allowed	315,956.89	
Additional deduction	929,491.32	
Total deductions		1,368,595.48
Net income for 1918 claimed by taxpayer		2,452,548.15

INVESTED CAPITAL

Invested capital as shown in office letter dated December 23, 1925		4,729,176.15
Addition:		
(a) Intercompany loss on sale of locomotive		10,000.00
Total		4,739,176.15
52a (b) 1917 income tax—		
Income tax deducted in office letter dated December 23, 1925	$659,110.79	
Tax liability as corrected $878,357.41 effective 200 days	481,291.73	
Amount restored to invested capital		177,819.06
Invested capital as corrected		4,916,995.21

PROOF OF INVESTED CAPITAL

Capital stock		$2,573,500.00
Surplus		2,403,548.90
Reserves		372,197.09
Total, beginning of year		5,349,245.99
Additions:		
Capital stock sales		45,369.86
Intercompany loss (1917)		10,000.00
Total		5,404,615.85
Reductions:		
1917 income tax	$481,291.73	
Additional tax (1916)	6,328.91	
Total reductions		487,620.64
As shown above		4,916,995.21

Computation of tax, 1918 rates

		Income	Tax
Excess profits tax:			
	Net income, taxable year	$2,452,548.15	
53a	Less excess profits credit	396,359.62	
	Balance	$2,056,188.53	
	Taxable at 30%	587,039.42	
			$176,111.83
	Taxable at 65%	$1,469,149.11	954,946.92
	Excess profits tax		$1,131,058.75
War profits tax:			
	Net income, taxable year	$2,452,548.15	
	Less war profits credit	563,150.34	
	Taxable at 80%	$1,889,397.81	$1,511,518.25
	Less excess profits tax		1,131,058.75
	War profits tax		$380,459.50
	Total excess profits and war profits tax		$1,511,518.25
Income tax:			
	Net income, taxable year	$2,452,548.15	
	Less—		
	Interest on United States obligations not exempt $17,819.46		
	War profits and excess profits tax 1,511,518.25		
	Exemption 2,000.00	1,531,337.71	
	Taxable at 12%	$921,210.44	110,545.25
54a	Total war profits, excess profits and income taxes if plaintiff's claims are allowed in full and profits tax computed under section 301 of the 1918 revenue act		$1,622,063.50

1920

NET INCOME

Net income	$1,529,710.37
Addition: (a) Excessive depreciation on account of revision of amortization allowances in prior years	99,553.04
Net income as corrected	$1,629,263.41

INVESTED CAPITAL

Invested capital		$7,649,707.81
Additions:		
(a) Profit on sale of dock (1917)	$6,426.45	
(b) Depreciation disallowed (1919)	339,038.27	
(c) Income tax prior years	413,437.41	
(d) Obsolescence disallowed (1918 and 1919)	259,278.04	
Total increase		1,018,180.17
Total		$8,667,887.98
Decreases:		
(e) Income tax 1919 prorated	$122,647.70	
(f) Miscellaneous revenue reserves	72,209.36	
(g) Loss on sale of locomotive (1917)	10,000.00	
(h) Paid-in surplus (contracts)	1,275,000.00	
55a (i) Inadmissibles	7,727.91	
Total decrease		1,487,584.97
Invested capital as corrected		$7,180,303.01

PROOF OF INVESTED CAPITAL

Capital stock		$2,623,500.00
Surplus as amended		5,102,393.57
Reserves		420,751.44
Premiums on capital stock		20,000.00
Capital surplus (Harbor Land Company)		464.36
Surplus from Armstrong Fuel Company		11,434.83
Total as corrected, beginning of year		$8,238,544.20
Additions:		
Capital stock sold (January 15, 1920, par)	$25,000.00	
Premium	20,000.00	
Total effective 352 days	$45,000.00	43,278.69
Total		$8,281,822.89
Reductions:		
Income tax (1919)	$416,194.66	
Additional income tax, prior years	553,720.26	
Dividends paid January 10, 1920, ($127,000.00)	123,877.05	
Inadmissibles	7,727.91	
Total reductions		1,101,519.88
Invested capital as above		$7,180,303.01

56a

COMPUTATION OF TAX

Excess profits tax:	
Net income	$1,629,263.41
Invested capital	$7,180,303.01
8% of invested capital	$574,424.41
Exemption	3,000.00
Total excess profits credit	$577,424.41

	Income	Credit	Balance	Rate	Tax
20%	$1,436,060.60	$577,424.41	$858,636.19	20%	$171,727.24
Balance	193,202.81		193,202.81	40%	77,281.12
Totals	$1,629,263.41	$577,424.41	$1,051,839.00		$249,008.36

Income tax:			
Net income		$1,629,263.41	
Less—			
Interest on United States Obligations not exempt	$80,253.71		
Excess profits tax	249,008.36		
Exemption	2,000.00		
		331,262.07	
Taxable at 10%		$1,298,001.34	129,800.13
Total excess profits and income tax			$378,808.49
Amount previously paid			324,660.92
Balance due			$54,147.57

57a [Omitted.]

64a In United States District Court

Plaintiff's reply

Filed Jan. 14, 1929

And now comes the Diamond Alkali Company, a corporation, the above-named plaintiff, and replies as follows to the new matter alleged in defendant's affidavit of defense:

65a I

9. Plaintiff denies that its correct amortization allowance for 1918 as a deduction from gross income for that year was $315,956.89, and avers that its lawful deduction from gross income for said year on account of amortization of war-time facilities was $1,245,448.21, and further avers that the plaintiff's amortization allowance was determined at $1,344,465.15 as alleged in the statement of claim.

Plaintiff denies that this court is without jurisdiction as alleged by defendant, and avers that this court has full jurisdiction in the premises.

10. Plaintiff denies that said additional tax, except $26,117.06 thereof, arose from the reduction of plaintiff's invested capital in the further sum of $1,030,321.28 or any further sum whatsoever and reavers by reference the facts set out in paragraph 10 of the statement of claim.

II

12. Plaintiff denies that the function of said amortization section was only to make investigations, examinations, and recommendations as to the allowance or amortization claims or that such claims, when approved by the chief or acting chief of said amortization section and notified to the taxpayer, were subject to further audit or review by the Bureau of Internal Revenue, and avers that an allowance approved by the chief or acting chief of the amortiza-
66a tion section as described in the statement of claim was a final determination by the commissioner as to amortization allow-

ance. Plaintiff denies on information and belief that said chief or acting chief had no power or authority to determine the amount of such allowances, and while admitting that the power to determine such allowances was and is vested in the Commissioner of Internal Revenue, avers that the said commissioner acts and at all times has acted through his subordinates, is not and never has been able to make such determinations personally, and on information and belief avers that the chief or acting chief of said amortization section had full power and authority to make determinations of amortization allowances as alleged in paragraph 12 of the statement of claim. Plaintiff denies that the said chief or acting chief made merely a report or recommendation that was subject to further audit and review, and avers on information and belief that said chief or acting chief made and was authorized to make final determinations of amortization allowances. Plaintiff denies that amortization allowances could not be made or become final without the approval of the commissioner personally or of the assistant to the commissioner, and avers on information and belief that as a matter of practice, well known to and acquiesced in by the commissioner, the final determinations of amortization allowances were made by the chief or acting chief of said amortization section and were notified of such to taxpayers and that the action by such acting chief as set out in the statement of claim was a final determination of the plaintiff's amortization allowance.

67a 13. Plaintiff denies that the correct amount of its amortization allowance was $387,224.40 and denies that $315,956.89 thereof was deductible from the plaintiff's gross income for 1918, and avers that the plaintiff's correct allowance was $1,756,453.64 and that $1,487,001.78 thereof was deductible from the plaintiff's gross income for 1918.

14. Plaintiff admits that the sole power of said Griffith was to investigate and make written report to said amortization section, but avers that his said report was a determination and upon approval by said B. L. Wheeler, Chief of Engineers, and approval by said T. J. S. Kishpaugh, acting chief of said amortization section, as described in the statement of claim, became and was a final determination of the plaintiff's amortization allowance.

15. Plaintiff admits that Griffith's said report to said amortization section constituted only a recommendation, but avers that the approval thereof by said B. L. Wheeler, Chief of Engineers, and said T. J. S. Kishpaugh, acing chief of said amortization section, as described in the statement of claim, constituted a final determination of the plaintiff's amortization allowance at the sum of $1,344,465.15 and that $1,245,448.21 thereof was deductible from 1918 gross income.

16. Plaintiff admits that Griffith's said report to said amortization section was a mere recommendation, but denies that the action
68a of said B. L. Wheeler was a mere approval of a recommendation, and avers that the action of said B. L. Wheeler, Chief

of Engineers, and T. J. S. Kishpaugh, acting chief of said amortization section, as described in the statement of claim, constituted a final determination of plaintiff's amortization allowance and was notified to the plaintiff as such.

17. Plaintiff denies the said report, when approved by said Wheeler and said Kishpaugh as described in the statement of claim, was a mere recommendation, or that the action of said Kishpaugh was a mere concurrence in a recommendation previously made, or that the action of said Kishpaugh was subject to further audit or review, and avers on the contrary that the said report, when approved by said Wheeler and said Kishpaugh as described in the statement of claim, became and was a final determination of the plaintiff's amortization allowance. Plaintiff denies on information and belief that said Kishpaugh was without authority to make a final determination, and avers on information and belief that said Kishpaugh, as acting chief of said amortization section, was fully authorized in the premises.

18. Plaintiff denies that its expression of willingness to accept said determination in the sum of $1,344,465.15 was conditioned on the closing of its case, and avers that said final determination was notified to the plaintiff as described in the statement of claim and was accepted by plaintiff without further objection and without any condition whatsoever upon the plaintiff's acceptance.

69a Plaintiff denies that said report appears on its face or otherwise to be a mere recommendation, denies that the same was subject to further audit, denies that the plaintiff was advised at the time of delivery or at any other time that the same was only a recommendation, and avers that said report, when approved as described in the statement of claim, became and was a final determination of the plaintiff's amortization allowance and was notified to and accepted by the plaintiff as such.

19. Plaintiff denies that in briefs or otherwise it requested further adjustments in its said amortization allowance as determined at $1,344,465.15 and avers that its said briefs had express reference to the commissioner's subsequent alleged redeterminations and contained protests against the same. Plaintiff denies that the first reexamination of said return with respect to said allowance was begun in 1921 and had not been completed on March 3, 1924, and was not completed until several years thereafter, and avers on the contrary that prior to March 3, 1924, the commissioner made final determination of the plaintiff's amortization allowance at $1,344,465.15 as alleged in the statement of claim and subsequent to March 3, 1924, instituted new reexaminations and attempted to make new determinations. Plaintiff denies that its amortization allowance was never determined at $1,344,465.15 and avers that its said allowance was determined at $1,344,465.15 as averred in the statement of claim. Plaintiff denies that its claim for amortization

70a allowance was from the year 1921 to a time long subsequent to March 3, 1924, in process of audit or investigation or con-

sideration, and avers that after the final determination of the plaintiff's amortization allowance by said T. J. S. Kishpaugh as described in the statement of claims until on or about October 1, 1924, no further proceedings were had or taken with respect to plaintiff's amortization allowance, and that on or about October 1, 1924, a new examination was ordered, which, however, was not begun until on or about April 1, 1925. Plaintiff avers that the commissioner's original determination and his two subsequent attempted redeterminations were successive, and denies that the commissioner's action or attempted action in respect to plaintiff's amortization allowance had the element of continuity. Plaintiff denies that its said claim was continuously in process of audit, and avers that a final determination was made by T. J. S. Kishpaugh, acting chief of said amortization section, who acted on behalf of the Commissioner of Internal Revenue, on or about the 2d day of December, 1921. Plaintiff denies that no determination was made until approval of the allowance by the assistant to the commissioner on or about July 11, 1927, and avers that a final determination was made on or about the 2d day of December, 1921, and that the said two subsequent attempted determinations were, as stated in their titles, attempted redeterminations.

20. Plaintiff denies that said further examination was a continuance of any examination or audit theretofore begun, and avers
71a that the same was a new examination. Plaintiff denies that there was only one examination or investigation of the plaintiff's return which was commenced prior to March 3, 1924, and ended subsequent thereto, and avers that plaintiff's amortization allowance was determined on or about December 2, 1921, as aforesaid and that the attempted subsequent redeterminations were *de novo*. Plaintiff denies that said report of Luce was a mere recommendation subject to further review or appears to be such on its face, and avers that the same was sent and noticed to the plaintiff as an attempted redetermination.

21. Plaintiff denies that said paper entitled "Second Redetermination of Amortization Claim" was a mere recommendation, or was subject to further review, or appeared on its face to be subject to further review, and avers on information and belief that the same was an attempted redetermination of the plaintiff's amortization allowance.

22. Plaintiff denies that it was entitled to an amortization deduction of only $315,956.89 for 1918, and avers that it was and is entitled in law and in fact to an amortization deduction from gross income of 1918 in the sum of $1,245,448.21 pursuant to said orginal determination.

23. Plaintiff admits that the commissioner undertook or attempted to make a determination of its amortization allowance at $387,224.40, of which $315,956.89 was a deduction from gross income for

1918, but avers that such attempted determination was an
72a attempted redetermination after expiration of the statutory period of limitation therefor and was void and of no effect. Plaintiff denies that said reports were mere recommendations, and avers that when the same were approved by the chief or acting chief of said amortization section they became and were determinations by the commissioner. Plaintiff denies that said two subsequent attempted determinations were based on new or additional evidence, except plaintiff admits that said Luce's examination was subsequent to said Griffith's and therefore included observation of production at plaintiff's plant over a period of time not yet elapsed when said Griffith's erred in his report to the extent that he did not allow plaintiff's claim of $1,756,453.64 in full, but denies other errors as alleged by defendant and avers that said Griffith's report was otherwise correct in amount of the allowance as approved by said acting chief of said amortization section. Plaintiff denies that said Griffith's report was based on the assumed fact that several plant units of plaintiff were no longer required by plaintiff in the operation of its business whereas the truth was that said plant units were only temporarily idle at the time of said Griffith's examination and were in fact required by the plaintiff, and avers that the report of said Griffith was not predicated on disused plant units, but on the ratio of post-war needs or requirements of plant to entire plant available. Plaintiff admits that said Griffith's investigations and report were made during a period of temporary business depression, but denies
73a that said fact prevented the said Griffith from ascertaining the plaintiff's plant requirements during the postwar period. Plaintiff denies that it was discovered on subsequent investigation or otherwise that the cost upon which said Griffith had recommended amortization was in excess of the true cost, and avers that, on the contrary, neither of the said subsequent attempted redeterminations indicated any error in the costs upon which amortization was claimed. Plaintiff avers that said two subsequent attempted redeterminations were erroneous in fact and void in law.

IV

29. Plaintiff denies on information and belief that any of the corporations used by the Commissioner of Internal Revenue as comparatives was a corporation engaged in a like or similar trade or business to that of the plaintiff or was a representative corporation engaged in such like or similar trade or business. As to defendant's averment that said corporations used as comparatives were as nearly as might be similarly circumstanced to plaintiff with respect to gross income, net income, profits per unit of business transacted, capital employed, amount and rate of war profits and excess profits, and all other relevant facts and circumstances, plaintiff avers that it has no knowledge or specific information in regard thereto, that the

Commissioner of Internal Revenue has at all times refused to disclose to the plaintiff the names of said corporations or any of said circumstances of any of them, and that said commissioner is
74a the plaintiff's sole source of information on the subject, but that from the plaintiff's general information as to computation of tax liability under said sections 327 and 328 and its knowledge of the tax liability resulting from applying to the plaintiff whatever comparatives the commissioner did apply, the plaintiff believes and expects to be able to prove at the trial of this cause that said averments are untrue. Plaintiff therefore denies that any of said corporations was as nearly as might be similarly circumstanced to the plaintiff with respect to gross income, or net income, or profits per unit of business transacted, or capital employed, or amount or rate of war profits or excess profits, or any other relevant fact or circumstance.

30. Plaintiff denies on information and belief that any of said corporations used by the commissioner as comparatives was engaged in a like or similar trade or business to that of the plaintiff in 1918 or that said four named corporations or any of them were not corporations whose invested capital could be satisfactorily determined under said section 326. Plaintiff denies on information and belief that said four corporations or any of them were not corporations engaged in a similar trade or business to that of the plaintiff or as nearly as might be similarly circumstanced to the plaintiff in the particulars and each of the particulars specified by the defendant and in all other relevant facts or circumstances, and avers, also on information and belief, that said four corporations alone were in 1918 engaged in a like or similar trade or business to that of the
75a plaintiff and were as nearly as might be similarly circumstanced to the plaintiff in all relevant facts and circumstances.

33. Plaintiff denies that the action of said commissioner in applying comparatives to the plaintiff under the circumstances of this case was or is discretionary and denies that this court is without jurisdiction to review the action, discretionary or otherwise, of said commissioner in applying comparatives under said section 328. To the contrary, plaintiff avers that the court has full jurisdiction in the premises.

34. Plaintiff denies that the court is without power or authority or jurisdiction or facilities to compute plaintiff's excess-profits tax for 1918 under said section 328, and avers that the court has full power, authority, and jurisdiction in the premises and that all necessary facilities will be supplied at the trial in the form of evidence, as to comparatives within the provisions of said section 328.

35. Plaintiff denies the averments of paragraph 35.

V

76a DEFENDANT'S FIRST SEPARATE DEFENSE

43. Plaintiff denies the averments of paragraph 43 and avers that the court has full jurisdiction in the premises.

44. Plaintiff denies the averments of paragraph 44.

DEFENDANT'S SECOND SEPARATE DEFENSE

45. Plaintiff denies the averments of paragraph 45, which averments are pleaded by reference.

46. Plaintiff denies the conclusion of law averred in paragraph 46, and for further reply thereto avers that the abnormalities referred to in paragraph 27 of the statement of claim were abnormalities of capital.

47. Plaintiff admits that depreciation is not allowed on the same cost as that upon which amortization is allowed and that an increase in plaintiff's deduction for amortization in 1918 will operate to reduce plaintiff's depreciation deduction for 1918. Plaintiff denies that there is or will be any necessity for any computation or recomputation or reduction of its invested capital, and avers that the
77a abnormalities on which the Commissioner of Internal Revenue has heretofore granted special assessment under sections 327 and 328 of the revenue act of 1918 are abnormalities of capital and will remain wholly unaffected by any change in income and that when the tax is computed under said sections the plaintiff's invested capital is immaterial for the computation is by percentage of income and without reference to invested capital of the plaintiff.

48. Plaintiff does not deny that computation of its tax under section 301 would reduce the amount recoverable in this action, but does deny that there is any basis whatsoever for computation of tax under said section, reavers by reference the averments of paragraph 27 of the statement of claim, and avers that the abnormalities in said paragraph 27 referred to were and are abnormalities of capital. Plaintiff denies the correctness of said Exhibit 2, and avers that the correct computation of plaintiff's tax liability for 1918, if such tax could lawfully be computed under said section 301, is shown in Exhibit A hereto attached and hereby made part hereof, and that the correct computation of plaintiff's tax liability for 1920 is set out in Exhibit 1 attached to and made a part of the plaintiff's statement of claim.

78a SMITH, SHAW & MCCLAY,
Attorneys for the Plaintiff.

79a [*Duly sworn to by W. E. Jones; jurat omitted in printing.*]

Exhibit A to reply

1918

Net income		$2,452,548.15
Invested capital		5,070,969.01
Excess profits tax credit		408,677.52
War profits tax credit		578,547.72

EXCESS AND WAR PROFITS TAX

Net income	$2,452,548.15	
Less war profits credit	578,547.72	
Taxable @ 80%	$1,874,000.43	$1,499,200.34

80a INCOME TAX

Net income		$2,452,548.15	
Liberty bond int.	17,819.46		
War & excess prof. tax	1,499,200.34		
Exemption	2,000.00		
		1,519,019.80	
Taxable @ 12%		933,528.35	112,023.40
Total tax liability			$1,611,223.74

In United States District Court

Motion to amend statement of claim

Filed Jan. 15, 1929

And now, to wit, January 15, 1929, comes the plaintiff, by its attorneys, Smith, Shaw & McClay, John W. Davis of counsel, and moves to amend its statement of claim heretofore filed by filing the annexed "Amendments to statement of claim."

JOHN W. DAVIS,
SMITH, SHAW & MCCLAY,
Attorneys for Plaintiff.

ORDER

And now, to wit, January 15, 1929, on consideration of the foregoing motion, the within amendments allowed and ordered filed.

Per Curiam,
G.

81a In United States District Court

Amendments to statement of claim

And now comes the plaintiff, by its attorneys, Smith, Shaw & McClay, and amends its statement of claim heretofore filed, as follows:

By striking out the introductory paragraph of said statement of claim and substituting therefor the following:

"Diamond Alkali Company, the above named plaintiff, has a claim against D. B. Heiner, collector of internal revenue for the twenty-third district of Pennsylvania, defendant, for the sum of $1,400,016.18, with interest thereon from November 15, 1927, upon a cause of action whereof the following is a statement:"

By striking out paragraph 5 of said statement of claim and substituting therefor the following:

"5. By letter dated July 11, 1927, the Commissioner of Internal Revenue (hereinafter called the 'commissioner') notified the plaintiff that its said returns were erroneous; that he, the commissioner, had made divers changes and adjustments in the plaintiff's tax liability and in the figures on which the same was computed; and that as the result of such changes and adjustments plaintiff owed to the Government of the United States in addition to the taxes previously paid as aforesaid, income and profits taxes of $1,215,615.14 for 1918 and $60,769.03 for 1920, or the total sum of $1,276,384.17. In and by said letter the commissioner notified the plaintiff further
82a that the plaintiff had theretofore overpaid its income and excess profits taxes for 1919 by the sum of $1,467.64."

By striking out paragraph 6 of said statement of claim and substituting therefor the following:

"6. Pursuant to said letter, and on or about the first day of November, 1927, the commissioner, notwithstanding the plaintiff's protests, proceeded to assess against the plaintiff alleged additional income and profits taxes of $1,215,615.14 for 1918 and $60,769.03 for 1920. At or about the same time, the commissioner issued certificate of overassessment for 1919 in said sum of $1,467.64."

By striking out paragraph 7 of said statement of claim and substituting therefor the following:

"7. On or about November 7, 1927, this defendant, instead of refunding to the plaintiff said sum of $1,467.64 overpaid by the plaintiff for 1919 and covered by said certificate of overassessment, seized and confiscated the same and applied said amount of $1,467.64 in part payment of said alleged additional tax of $1,215,615.14 for 1918, and on or about the same date the defendant served upon the plaintiff written notice of said assessments and demand for payment of said alleged additional taxes (giving credit of $1,467.64 on said alleged additional tax of $1,215,615.14 for 1918), together with interest of $117,739.08 on said alleged (net) tax of $1,214,147.50 for 1918
83a and interest of $5,892.93 on said alleged tax of $60,769.03 for 1920, or the total sum of $1,398,548.54, and defendant accompanied his demand with threats of penalties, further interest, and seizures of the plaintiff's property if payment should not be made within ten days."

By striking out paragraph 9 of said statement of claim and substituting therefor the following:

"9. (a) All of said alleged additional tax for 1918 with interest thereon was assessed and collected and paid under protest more than five years after the return for 1918 was filed and after the statutory period of limitation within which the commissioner and the defendant were permitted by law to make such assessment and collection.

"(b) The said alleged additional tax for 1918 (except $188,387.39 thereof, which, however, plaintiff does not admit was owing), irrespective of the statute of limitations, resulted from the action of the commissioner as follows:

"(1) Redetermination of plaintiff's allowance for the amortization of war-time facilities for the years 1918 and 1919 under section 234 (a) (8) of the revenue act of 1918 in the sum of $387,224.40 instead of permitting the same to stand at $1,344,465.15 as determined at the time and in the manner hereinafter described; whereby the plaintiff's deduction from 1918 gross income on account of said allowance was changed from $1,245,448.21 to $315,956.89.

84a "(2) Disallowance of $439,104.16 of the total deduction, to wit, $876,366.71, taken by the plaintiff from gross income on its books and on its returns for 1918 on account of wear, tear, exhaustion, and obsolescence of its depreciable physical assets.

"(3) Determination of 54.54+% under section 328 of the revenue act of 1918 as the ratio of plaintiff's excess profits tax to its net income instead of 45% as demanded by the plaintiff."

By striking out paragraph 11 of said statement of claim and substituting therefor the following:

85a "11. Said action of the commissioner and the defendant in assessing and collecting the aforesaid alleged additional taxes with interest thereon more than five years after the returns for 1918 and 1920 respectively were filed and after the statutory periods within which the commissioner and the defendant were permitted by law to assess and collect any additional taxes for 1918 or 1920 was and is in all respects erroneous, illegal, and void. Furthermore, said above described adjustments by the commissioner, irrespective of the bar of the statute of limitations, were erroneous and illegal in all respects and said alleged additional taxes and the assessment and collection thereof and of interest thereon were and are erroneous, illegal, and void. Annexed hereto, marked Exhibit 1, and made a part hereof is a computation and statement of plaintiff's income and profits tax for 1918 and 1920 showing the amounts that would be owing, except for the bar of the statute of limitations, the amounts that plaintiff was compelled to pay, and the amounts of alleged taxes and interest paid by the plaintiff in excess of the amounts that would be owing, except for the bar of the statute of limitations, but plaintiff does not by said Exhibit 1 or otherwise admit that any part of the alleged additional taxes and interest for 1918 and 1920 were or are owing."

By striking out paragraph 40 of said statement of claim and substituting therefor the following:

86a "40. The said alleged additional taxes for 1918 and 1920 and the interest thereon paid by the plaintiff as hereinabove stated, and the assessment and collection thereof, were in all respects erroneous, illegal, and void."

By striking out paragraph 42 of said statement of claim and substituting therefor the following:

"42. No part of said overpayments of taxes and interest has been repaid or refunded to the plaintiff, and the defendant is indebted to the plaintiff as follows:"

[*Duly sworn to by W. E. Jones; jurat omitted in printing.*]

Year	Tax overpaid	Interest overpaid
1918	$1,215,615.14	$117,739.06
1920	60,769.03	5,892.93

By striking out the concluding sentence of said statement of claim, beginning with the word "wherefore," and substituting therefor the following:

"Wherefore this suit is brought and plaintiff claims judgment against the defendant for the sum of $1,400,016.18, with interest thereon from November 15, 1927."

SMITH, SHAW & MCCLAY,
Attorney for Plaintiff.

87a In United States District Court

Plaintiff's reply to affidavit of defense to plaintiff's amendments to its statement of claim

Filed Jan. 21, 1929

And now comes the above-named plaintiff, Diamond Alkali Company, a corporation, by its attorneys, Smith, Shaw & McClay, and makes reply to the new matter alleged in the affidavit of defense to plaintiff's amendments to its statement of claim:

88a–89a [Omitted.]

90a (b) Plaintiff denies that said amortization allowance was correctly determined at $387,224.40 and denies that the correct deduction from plaintiff's gross income for 1918 on account of amortization was $315,956.89, and avers that the plaintiff's correct amortization allowance and the portion thereof properly deductible from the plaintiff's gross income for 1918 are as stated in the plaintiff's statement of claim heretofore filed.

Plaintiff denies that the commissioner's disallowance of $439,104.16 of the plaintiff's depreciation deduction for 1918 was proper, and

avers that the wear, tear, exhaustion, and obsolescence actually sustained by the plaintiff in 1918 and properly deductible from the plaintiff's gross income for 1918 was $876,366.71.

91a Plaintiff denies that the court is without jursidiction as alleged by defendant, and avers that it has full jurisdiction in the premises.

10. Plaintiff denies that prior to March 15th, 1926, or at any other time it consented, either by written instruments or otherwise, to extend, or by itself had power to extend, the period within which determination or assessment or collection of its 1920 taxes might lawfully be made, and denies that the taxes herein sought to be recovered were determined or assessed or collected prior to expiration of the period within which such determination, assessment, or collection might lawfully have been made. Plaintiff repleads by reference its denials and averments made in paragraph 9 (a) hereof with respect to said written instruments Exhibit 3 annexed to defendant's affidavit of defense.

Plaintiff denies that said additional tax (except $26,771.06 thereof) arose out of reduction of plaintiff's invested capital in the further sum of $1,030,321.28 or any further sum whatsoever and repleads by reference the averments of the statement of claim in respect to the reduction of the plaintiff's invested capital.

11. Plaintiff denies that its tax liability for 1918 or 1920 was as stated by the defendant and avers that its true tax liability for said years is as alleged in the statement of claim.

92a Plaintiff denies that said computation attached to defendant's affidavit of defense is correct and avers that the plaintiff's true and correct tax liability for said years is as shown in Exhibit I annexed to and made a part of the plaintiff's statement of claim.

93a SMITH, SHAW & MCCLAY,
Attorneys for Plaintiff.

[*Duly sworn to by W. E. Jones; jurat omitted in printing.*]

94a In United States District Court

Affidavit of defense to amendments to statement of claim

Filed Jan. 21, 1929

Comes now D. B. Heiner, defendant above named, and says that he has a just, true, legal, and full defense to all of the allegations contained in the amendments to the statement of claim, and that the nature and character of that defense is as follows:

Paragraphs five, six, and seven of the amendments to statement of claim are admitted.

95a

IX

Answering the allegations contained in paragraph 9 (b) of plaintiff's amendments to statement of claim, defendant admits that said alleged additional tax for 1918 (except $188,387.39 thereof), irrespective of the statute of limitations, resulted from the action of the commissioner as follows:

96a 1. Determining plaintiff's allowance for amortization of war-time facilities for the years 1918 and 1919 under section 234 (a) (8) of the revenue act of 1918 in the sum of $387,224.40 instead of permitting the same to stand at $1,344,465.15, whereby plaintiff's deduction from 1918 gross income on account of said allowance was changed from $1,245,448.21 to $315,956.89.

2. Disallowance of $439,104.16 of the total deduction of $876,366.71 taken by the plaintiff from gross income on its books and on its returns for 1918 on account of wear, tear, exhaustion, and obsolescence of its depreciable physical assets; and

3. Determining of 54.54+% under section 328 of the revenue act of 1918 as the ratio of plaintiff's excess-profits tax to its net income instead of 45% as demanded by the plaintiff.

Defendant denies that plaintiff's said allowance for amortization was ever determined in the sum of $1,344,465.15, and alleges that the said allowance was correctly determined in the amount of $387,224.40 and that plaintiff's correct allowance for the year 1918 as a deduction from its gross income for said year on account thereof was $315,956.89. Defendant denies that $876,366.71 represents the true and correct deduction allowable to plaintiff because of wear, tear, exhaustion, and obsolescence of its depreciable physical

97a assets, and on the contrary, alleges that the Commissioner of Internal Revenue properly disallowed $439,104.16 of the total deduction claimed.

Defendant further alleges that this court is without jurisdiction to review the action of the Commissioner of Internal Revenue in computing and determining plaintiff's excess-profits taxes for said years, or either of them, under sections 327 and 328 of the revenue act of 1918, and is without jurisdiction to recompute or to determine at all plaintiff's excess-profits tax at 54.54%, or any percentage of its income or revised income for the year 1918 under said sections 327 and 328 of the revenue act of 1918.

98a

XI

In answer to the allegations contained in paragraph 11 of plaintiff's amendments to the statement of claim, defendant denies that said action of the commissioner in assessing and collecting the aforesaid alleged additional taxes with interest thereon more than five years after the returns for 1918 and 1920, respectively, were filed, was erroneous, illegal, and void, and alleges that the acts of the said commissioner and this defendant were in all respects valid and lawful.

Defendant denies that said taxes were assessed and collected after the statutory period within which the commissioner and the defendant were permitted by law to assess and collect the same, and alleges
99a that said taxes were assessed and collected within the period provided therefor by law. Defendant denies that the above-described adjustments by the commissioner, irrespective of the bar of the statute of limitations, were erroneous and illegal in all respects, and alleges that the said adjustments and the assessment and collection of said taxes with interest were in all respects legally and lawfully made. Defendant denies that Exhibit 1, attached to the said amendments to plaintiff's statement of claim, is a correct computation or statement of plaintiff's income and profits tax for 1918 and 1920, showing the amounts that would be owing except for the bar of the statute of limitations, and alleges that plaintiff's income and excess-profits taxes for the years 1918 and 1920, respectively, were determined and lawfully assessed against the plaintiff and collected from it in the following respective amounts: $2,390,264.25 for 1918 and $324,660.92 for 1920; and alleges that a true and correct computation and statement of plaintiff's income and profits tax liability for the years 1918 and 1920 is attached to and made a part of defendant's original affidavit of defense and is by this reference made a part hereof.

XL

In answer to paragraph 40 of the amendments to plaintiff's statement of claim defendant denies that the said alleged additional tax for 1918 and 1920 and interest thereon paid by the plaintiff, and the assessment and collection thereof were, in all respects, erroneous,
100a illegal, and void, and alleges that the acts of the commissioner and the defendant in assessing and collecting the same were, in all respects, legal and valid.

XLII

In answer to paragraph 42 of the amendments to plaintiff's statement of claim, defendant admits that no part of the alleged overpayments of taxes and interest has been repaid or refunded to plaintiff. Defendant denies, however, that he is indebted to the plaintiff in the sums set out in paragraph 42 or in any sum whatever.

D. B. HEINER,
Defendant.

101a [*Duly sworn to by D. B. Heiner; jurat omitted in printing.*]

Summons

United States District Court

Western District of Penna.

The President of the United States of America

To the Marshal of the Western District of Penna.—Greeting:

You are hereby commanded that you summon D. B. Heiner, coll. of internal revenue, late of your district, if he may be found therein, so that he be and appear 15 days after service of this summons before the United States District Court for the Western Dis-
102a trict of Penna., at Pittsburgh, on the first Monday of Sept. next to answer to Diamond Alkali Company, a corporation in an action of assumpsit. And have you then and there this writ.

Witness, the honorable the United States district judges at Pittsburgh, this 25th day of August, A. D. 1928.

[SEAL.] J. WOOD CLARKE,
Clerk.

RETURN ON SERVICE OF WRIT

UNITED STATES OF AMERICA,
Western District of Penna., ss:

I hereby certify and return that I served the annexed summons on the therein-named D. B. Heiner, collector of internal revenue, by handing to and leaving a true and attested copy thereof with D. B. Heiner personally at Pittsburgh in said district on the 27th day of August, A. D. 1928.

Service $2.00.

JAMES C. MCGREGOR.
U. S. Marshal.
By JOE H. IROIP, *Deputy.*

103a In United States District Court

Certificate of probable cause

And now, on this 23rd day of April, A. D. 1930, the court, having been fully advised in the premises, hereby certifies that inasmuch as the collector of internal revenue was acting pursuant to instructions from the Commissioner of Internal Revenue, there was probable cause for the collection of Federal taxes and interest thereon from the plaintiff, as shown by the record in this cause.

Per Curiam.

G.

In United States District Court

Plaintiff's petition for appeal

Filed April 23, 1930

To the honorable the Judges of said Court:

The plaintiff, Diamond Alkali Company, a corporation, by its attorneys, Smith, Shaw, McClay & Seifert, conceiving itself aggrieved by the judgment made and entered in this court on the 14th day of February, 1930, in the above-entitled cause, does hereby appeal from said judgment to the United States Circuit Court of Appeals for the Third Circuit, for the reasons specified in the assignment of errors filed herewith, and prays that this appeal may be allowed and that a transcript of the record, proceedings, and papers upon
104a which said judgment was made and entered, duly authenticated, may be sent to the United States Circuit Court of Appeals for the Third Circuit.

SMITH, SHAW, MCCLAY & SEIFERT,
Attorneys for the Plaintiff.

In United States District Court

Order allowing appeal

And now, to wit, April 23, 1930, an appeal is allowed as prayed for in the foregoing petition. Bond for costs in the sum of five hundred ($500) dollars to be approved and filed.

R. M. GIBSON,
United States District Judge.

[Bond on appeal for $500 approved and filed April 23, 1930, omitted in printing.]

105a [Omitted.]

106a In United States District Court

Defendant's petition for appeal

Filed May 13, 1930

The defendant, D. B. Heiner, collector of internal revenue for the twenty-third district of Pennsylvania, by his attorneys, conceiving himself aggrieved by the judgment made and entered on the 14th day of February, A. D. 1930, in the above-entitled case, does hereby appeal from said judgment to the United States Circuit Court of Appeals for the Third Circuit, for the reasons specified in the assignments of error, which are filed herewith, and he prays that

this appeal may be allowed and that a transcript of the record, proceedings, and papers upon which said judgment was made and entered, duly authenticated, may be sent to the United States Circuit Court of Appeals for the Third Circuit.

LOUIS E. GRAHAM,
United States Attorney for the Western District of Pennsylvania,
JOHN A. McCANN,
Special Assistant to the U. S. Attorney,
Attorneys for the Defendant.

107a In United States District Court

Order allowing appeal

The foregoing petition for appeal is allowed this 13th day of May, A. D. 1930.

R. M. GIBSON,
District Judge.

In United States District Court

Plaintiff's assignments of error

Filed April 23, 1930

And now, to wit, this 23rd day of April, 1930, comes the plaintiff, Diamond Alkali Company, by its attorneys, Smith, Shaw, McClay & Seifert, and, together with its petition for appeal in the above-entitled cause, files assignments of error as follows:

First. The trial court erred in ordering judgment for the plaintiff for only $175,410.60, with interest, instead of judgment for a much larger amount, with interest, the order of the trial court in that behalf and the plaintiff's exception thereto being as follows:

"And now, to wit, February 14th, 1930, the foregoing motion having been presented in open court, upon consideration thereof and upon motion of the attorneys for the plaintiff, it is ordered that the judgment entered on February 10, 1930, herein, be vacated, and that judgment be entered for the plaintiff, Diamond Alkali Company, and against the defendant, D. B. Heiner, collector of internal revenue, in the amount of $175,410.60 with interest from November 15, 1927, as provided by law."

108a

Exception reserved to plaintiff and bill sealed.

Per Curiam.

G.

Second. The trial court erred in entering the following judgment pursuant to its said order excepted to by plaintiff:

"Feb. 14, 1930. Pursuant to the above order, judgment is hereby entered for the plaintiff, Diamond Alkali Company, and against the

defendant, D. B. Heiner, collector of internal revenue, in the amount of $175,410.60 with interest from Nov. 15, 1927."

J. WOOD CLARK,
Clerk.

Third. The trial court erred in refusing plaintiff's motion for judgment, which motion and the court's order refusing the same, and the plaintiff's exception thereto, are as follows:

"And now, January 23, 1929, comes counsel for plaintiff and moves the court that under the pleadings and all of the evidence in this case judgment must be entered for the plaintiff for the full amount of its claim."

JOHN W. DAVIS,
SMITH, SHAW, MCCLAY & SEIFERT,
Attorneys for Plaintiff.

109a *Order*

And now, to wit, February 14th, 1930, the foregoing motion having been presented in open court, upon consideration thereof and upon motion of the attorneys for the plaintiff, it is ordered that the judgment entered February 10, 1930, herein, be vacated, and that judgment be entered for the plaintiff, Diamond Alkali Company, and against the defendant, D. B. Heiner, collector of internal revenue, in the amount of $175,410.60 with interest from November 15, 1927, as provided by law.

Exception reserved to plaintiff and bill sealed.

Per Curiam.

G.

110–114a [Omitted.]

115a Sixth. The trial court erred in refusing plaintiff's offer of proof, which offer, the court's ruling thereon, and plaintiff's exception to such ruling were as follows:

"Mr. TEALL. The plaintiff offers to prove by the witness on the stand that during the years 1918 and 1920, and both of them, at (that) except for this plaintiff, the only persons or corporations engaged, in the United States, in the manufacture of alkali, or in a like or similar trade or business to that of this plaintiff, were the following: The Matheson Alkali Works, the Solvay Process Company, the Columbia Chemical Company, and the Michigan Alkali Company. This in connection with the point of special assessment which has been raised in the statement of claim.

"Mr. MCCANN. That is objected to as incompetent, irrelevant, and immaterial, and on the further ground that the court is without power to review actions of the commissioner in determining special assessments.

"Mr. TEALL. And we offer at the same time to produce other witnesses to corroborate this witness on the point that I have mentioned and to prove that the Commissioner of Internal Revenue,

in determining the special assessment rate, did not use
116a these corporations, or any of them, as comparatives, and that the average ratio of excess-profits tax and war-profits tax to income over and above the exemption of $3,000 was, for the corporations I have named, 28% for the year 1918 and less than that for the year 1919.

"Mr. McCann. The same objection, your honor."

Objection sustained. Exception noted to plaintiff.

Seventh. The trial court erred in refusing plaintiff's offer of proof, which offer, the court's ruling thereon, and plaintiff's exception to such ruling were as follows:

"Mr. Teall. The plaintiff offers to prove by the witness on the stand that the abnormalities upon which the commissioner determined and so declared of record, entitled this corporation to special assessment for the years for which special assessments were allowed, were abnormalities of capital and not abnormalities of income. This for the purpose of showing that irrespective of any changes in income that this court may allow, the plaintiff is still entitled to special assessment, because the abnormalities continued through all the years.

"Mr. McCann. We note an objection on the ground that it
117a is incompetent, irrelevant, and immaterial, and is a direct attempt to go into the question of special assessment, which has already been ruled upon by the court adversely to the plaintiff, and that it is an attempt to go into an act which has been performed by the Commissioner of Internal Revenue, pursuant to the discretion confided in him by Congress, under sections 327 and 328 of the revenue act of 1918."

Objection sustained. Exception noted to plaintiff.

118a–119a [Omitted.]

120a Seventeenth. The trial court erred in making the following finding of fact, being a portion of its 19th finding of fact:

"19. * * * The cost of these facilities to the plaintiff, after depreciating to January 1, 1918, those installed during 1917, was $2,108,361.40."

Eighteenth. The trial court erred in making the following finding of fact:

"20. A schedule of all of the aforesaid facilities, with the 1917 and 1918 costs, less depreciation, except a limestone dock costing $340,000, appears in the second column of Schedule I attached to defendant's Exhibit F, received in evidence at the trial. Said column is under heading '1917–1918 costs allowed less 1917 depreciation.' Said second column of Schedule I of defendant's Exhibit F, excepting the item opposite the words 'raw material equipment' is incorporated in these findings by reference with like effect as if herein fully set forth. The item opposite the words 'raw material equipment' is stricken out, however, and replaced by the entry '$559,215.03,' the

original entry being increased by $340,000, the cost of the limestone dock aforementioned."

Nineteenth. The trial court erred in making the following finding of fact:

"42. The capacity of each furnace at the end of the amortization period and during the postwar period was, under normal conditions,
121a 33,250 tons of soda-ash per month.

Twentieth. The trial court erred in making the following finding of fact:

"45. The 'value in use,' that is, the ratio of the actual use of the facilities to the use of which they were capable, during the postwar period is represented by the fraction 22597/33250, or 68%; and the percentage which represents the extent to which the facilities were not necessary for the postwar use is 32%."

Twenty-first. The trial court erred in making the following finding of fact:

"46. A reasonable deduction on account of the the amortization of plaintiff's war-time facilities acquired in 1917 and 1918 at a total cost (less depreciation of 1917 acquisitions) of $1,768,361.40, is $646,996.01. This amount should be spread over the year 1918 and the first three months of 1919, by allocating $553,957.98 to 1918 and $93,038.03 to 1919."

Twenty-second. The trial court erred in making the following finding of fact, which was included in its 47th finding:

"47. * * * This was a reasonable rate for that period."

Twenty-third. The trial court erred in refusing plaintiff's request for the following finding of fact:

"25. The plaintiff constructed, erected, installed, and ac-
122a quired between April 6, 1917, and March 31, 1919, inclusive, certain buildings, machinery, equipment, and other facilities for the production of articles contributing to the prosecution of the war against the German Government. The cost of these facilities to the plaintiff, after depreciating to January 1, 1918, those installed during 1917 was $3,099,988.83."

Twenty-fourth. The trial court erred in refusing plaintiff's request for the following finding of fact:

"26. A complete schedule of all the aforesaid facilities, the dates on which the expenditures for the same were made, the several costs of those acquired during 1917 as depreciated to January 1, 1918, and the several costs, without any adjustment for depreciation, of those acquired subsequent to December 31, 1917, are shown in plaintiff's Exhibit 7, received in evidence at the trial, which is incorporated in these findings by reference with like effect as if herein fully set forth.

Twenty-fifth. The trial court erred in refusing to make the following finding of fact included in plaintiff's 45th request:

"45. * * * The alkali manufactured by it during 1918 consisted of soda-ash or sodium carbonate and caustic soda. During

that year it began the installation of facilities to manufacture sodium bicarbonate, another alkali. The manufacture of these alkali products involved a commercial application of a chemical pro-
123a cess and required the employment of many facilities of various kinds. These facilities were connected, intermingled, interdependent, and interrelated. Numerous facilities were employed in each of the several steps required in the manufacturing process. The process of manufacture was continuous and all portions of the plant were required to be in operation, and were in operation, at all times. Chemical reagents were used for the purpose of effecting necessary chemical changes and were recovered in the later steps of the process to be used over again. The manufacturing process was thus not only continuous but was also rotary in character. The plant was balanced; that is, relatively there was neither an excess nor a shortage of facilities of any given kind or of facilities in any given step. When any portion of the plant operated at capacity all other portions operated substantially at capacity."

Twenty-sixth. The trial court erred in refusing plaintiff's request for the following finding of fact:

"46. The plant was one harmonious unit or whole. No part, department, or portion of the plant was severable, for purposes of operation or production, from the unit or whole.

Twenty-seventh. The trial court erred in refusing plaintiff's request for the following finding of fact:

124a "47. The extent of the use of the various facilities comprising the plant of the plaintiff could not be determined, estimated, or measured separately or by departments or by portions, but could only be determined as a unit or whole."

Twenty-seventh. The trial court erred in refusing plaintiff's request for the following finding of fact:

"52. The capacity of each furnace at the end of the amortization period and during the post-war period was, under normal conditions, forty tons of soda-ash per day, or 45,017 tons per month."

Twenty-ninth. The trial court erred in refusing plaintiff's request for the followng finding of fact:

"55. The 'value in use,' that is, the ratio of the actual use of the facilities to the use of which they were capable, during the post-war period is represented by the fraction 22,597/45,017, or 50.3%; and the percentage which represents the extent to which the facilities were not necessary for the post-war use is 49.7%."

Thirtieth. The trial court erred in refusing plaintiff's request for the following finding of fact:

"56. A reasonable deduction on account of the amortization of plaintiff's war-time facilities is 49.7% of their cost (1917 acquisitions depreciated as hereinbefore stated) or 49.7% of $3,099,988.83, which amounts to $1,540,694.49. This amount should be spread over
125a the year 1918 and the first three months of 1919 by allocating $1,427,222.34 to 1919 and $113,474.15 to 1919."

Thirty-first. The trial court erred in refusing plaintiff's request for the following finding of fact:

"57. A reasonable deduction for amortization of plaintiff's war-time facilities is not less than that found in the amortization report of the said Griffith approved December 1, 1921, namely $1,344,465.15, of which $1,245,448.21 is deductible from 1918 gross income and $99,016.94 is deductible from 1919 gross income."

Thirty-second. The trial court erred in holding that the plaintiff's amortization allowance should be $649,996.01, apportioned $553,957.98 to 1918 and $93,038.03 to 1919.

Thirty-third. The trial court erred in including in its 26th finding of fact the portion italicized as follows:

"26. On or about the 2nd day of December, 1921, a copy of said report and recommendation, with said indorsement thereon, was delivered to the plaintiff by said amortization section on behalf of and with the authority of the commissioner, *with an accompanying declaration to the effect that the amount of plaintiff's amortization deduction was tentatively, not finally, declared, and was subject to readjustment.*"

126a Thirty-fourth. The trial court erred in refusing plaintiff's request for the following finding of fact:

"32. At the time the said Griffith report came before the said Kishpaugh, as acting chief of the amortization section, the chief and acting chief of the said section were duly authorized by the commissioner to make final determinations of amortization deductions."

Thirty-fifth. The trial court erred in refusing plaintiff's request for the following finding of fact:

"33. In approving the report of Griffith, as previously approved by B. L. Wheeler, chief of engineers, the said Kishpaugh made a final determination of the amortization deduction of the plaintiff."

Thirty-sixth. The trial court erred in holding as matter of law that determination or redetermination of the plaintiff's amortization allowance subsequent to March 3, 1924, was not barred by section 234 (a) (8) of the revenue acts of 1918 and 1921, and in refusing to hold that such determination or redetermination was barred by said section of said acts.

Thirty-seventh. The trial court erred in holding that the Griffith report as indorsed and sent to the plaintiff was not a determination of plaintiff's amortization deduction allowance and in refusing to hold that the same was such determination.

127a Thirty-eighth. The trial court erred in making the following finding of fact:

"49. Plaintiff is not entitled to any sum for exhaustion, wear, tear, and obsolescence of its depreciable properties in addition to the amount allowed by the Comissioner of Internal Revenue, to-wit, $437,262.55."

Thirty-ninth. The trial court erred in refusing plaintiff's request for the following finding of fact:

"58. The plaintiff is entitled to a deduction for depreciation during 1918 computed on a cost basis of $4,513,760.20 * * *."

Fortieth. The trial court erred in refusing plaintiff's request for the following finding of fact:

"59. In determining the taxes of the plaintiff for 1917, 1918, 1919, and 1920, the commissioner found and used a rate of 10.4% per annum for wear, tear, exhaustion, and obsolescence (depreciation). This was a reasonable rate under normal conditions of labor, fuel, raw materials, and other relevant factors."

Forty-first. The trial court erred in not including in its 48th finding, or in any other finding, the following finding of fact, which the plaintiff included in its 60th request:

"60. * * * The plaintiff's labor turnover for that year—1918—was at least 600%.

128a Forty-second. The trial court erred in refusing plaintiff's request for the following finding of fact:

"61. As a result of the aforesaid conditions obtaining in 1918, the wear and tear upon the plaintiff's plant as a whole and especially upon machinery and apparatus was greatly increased. The wearing-out process of the plant as a whole was from two to three times as rapid as under normal conditions. Under the conditions obtaining in 1918, the plaintiff's plant, if new at the beginning of that year, would have had an average life of from four and one-half to five years."

Forty-third. The trial court erred in refusing plaintiff's request for the following finding of fact:

"62. Under the conditions obtaining in 1918, the plaintiff's capital invested in depreciable properties would have turned over every four and one-half to five years."

Forty-fourth. The trial court erred in refusing plaintiff's request for the following finding of fact:

"63. A reasonable rate for depreciation—that is, exhaustion, wear, tear, and obsolescence—of plaintiff's depreciable properties for 1918 was 23%. A reasonable allowance for depreciation for 1918 is 23% of $4,513,760.20, or $1,038,164.85."

Forty-fifth. The trial court erred in refusing plaintiff's request for the following finding of fact:

129a "64. A reasonable allowance for depreciation—that is, wear, tear, exhaustion, and obsolescence—of plaintiff's depreciable properties for the year 1918 is not less than the amount written off on its books and taken as a deduction on its return, namely, $876,366.71."

Forty-sixth. The trial court erred as matter of law in sustaining the depreciation deduction of $437,262.55 for 1918 and in not holding that plaintiff was entitled to a depreciation deduction for that year in the sum of $876,366.71.

Forty-seventh. The trial court erred as matter of law in holding that the plaintiff's evidence was insufficient to show that the deprecia-

tion deduction for 1918 allowed by the Commissioner of Internal Revenue was too low, and in not holding that the sufficient and uncontradicted evidence in the record showed the plaintiff to be entitled to a depreciation deduction for 1918 in the sum of $876,366.71.

Forty-eighth. The trial court erred in holding that it was without jurisdiction to review the special assessment rate used by the commissioner for 1918 or to hear evidence upon and fix the correct special assessment rate for that year.

SMITH, SHAW, MCCLAY & SEIFERT,
Attorneys for Plaintiff.

130a In United States District Court

Defendant's assignments of error

Filed May 13, 1930

Comes now the defendant, D. B. Heiner, collector of internal revenue for the twenty-third district of Pennsylvania, by his attorneys, and in connection with his petition for appeal in the above-entitled case, files the following assignments of error:

1. The court erred in rendering judgment for the plaintiff.

2. The court erred in failing to render judgment in favor of the defendant.

3. The court erred in applying the rate of 54.54% in determining plaintiff's war-profits and excess-profits tax for the year 1918

4. The court erred in applying the rate of 19.8% in determining plaintiff's war-profits and excess-profits tax for the year 1919.

5. The court erred in applying to the determination of plaintiff's war-profits and excess-profits taxes for the year 1918 the "special assessment" rate used by the Commissioner of Internal Revenue in granting the plaintiff relief under the provisions of sections 327 and 328 of the revenue act of 1918.

6. The court erred in applying to the determination of
131a plaintiff's war-profits and excess-profits taxes for the year 1919 the "special assessment" rate used by the Commissioner of Internal Revenue in granting the plaintiff relief under the provisions of sections 327 and 328 of the revenue act of 1918.

7. The court erred in failing to calculate plaintiff's war-profits and excess-profits taxes for the year 1918 for the purpose of this case, under the provisions of section 301 of the revenue act of 1918.

8. The court erred in failing to calculate plaintiff's war-profits and excess-profits taxes for the year 1919 for the purpose of this case. under the provisions of section 301 of the revenue act of 1918.

132a–140a [Omitted.]

141a 54. The court erred in including in its findings of fact (No. 56) the following:

"The plaintiff is entitled to judgment for the sum of $143,029.05, with interest thereon of $13,852.37, for overpayment of 1918 taxes,

and $16,891.21, with interest thereon of $1,637.97, overpayment of 1920 taxes, the total being $175,410.60, with interest thereon from the date of overpayment, to wit, November 15, 1927."

142a 55. The court erred in finding as a fact that (Finding No. 55):

"Exhibit 1, attached hereto and made part hereof, is a computation of the taxes for 1918 and 1920, after deducting for amortization of war facilities in 1918 the sum of $143,029.05; and after increasing the invested capital for 1920 by the sum of $574,372.90."

143a–162a [Omitted.]

163a Wherefore, defendant prays that the judgment rendered herein be reversed, with directions to the District Court of the United States for the Western District of Pennsylvania, to enter judgment in favor of the defendant below.

May 13th, A. D. 1930.

LOUIS E. GRAHAM,
United States Attorney for the Western District of Pennsylvania,
JOHN A. MCCANN,
Special Assistant to the U. S. Attorney,
Attorneys for the Defendant.

In United States District Court

Plaintiff's stipulation for printing record

Filed May 21, 1930

It is hereby stipulated by and between the parties hereto, acting by their respective attorneys, that the following be printed as and shall constitute the record on the pending appeal of the plaintiff to

164a the United States Circuit Court of Appeals for the Third Circuit in the above-entitled case:

1. Docket entries.
2. All pleadings.
3. Bill of exceptions, omitting therefrom, however, all tax returns of the plaintiff which were offered by defendant; order of settlement and allowance.
4. Petition for appeal, order allowing appeal, and appeal bond.
5. Assignments of error.
6. This stipulation.
7. Clerk's certificate.

MAYNARD TEALL,
SMITH, SHAW, MCCLAY & SEIFERT,
Attorneys for Plaintiff.

LOUIS E. GRAHAM,
United States Attorney.

W. J. AIKEN,
Assistant United States Attorney,
Attorneys for Defendant.

165a

In United States District Court

Defendant's stipulation for printing the record

Filed May 27, 1930

It is hereby stipulated and agreed by and between the parties hereto, by their respective counsel, that the following be printed as and constitute the record on the pending appeal of the defendant to the United States Circuit Court of Appeals for the Third Circuit, in the above-entitled case:

1. Docket entries.
2. All pleadings.
3. Stipulation that the matter contained in plaintiff's bill of exceptions shall constitute defendant's bill of exceptions, with order of settlement and allowance.
4. Petition for appeal and order allowing appeal.
5. Assignments of error.
6. This stipulation.
7. Clerk's certificate.

SMITH, SHAW, MCCLAY & SEIFERT,
Attorneys for the Plaintiff.
LOUIS E. GRAHAM,
United States Attorney,
W. J. AIKEN,
Assistant United States Attorney,
Attorneys for the Defendant.

166a [Clerk's certificate to foregoing transcript omitted in printing.]

1

In United States District Court

Stipulation as to bill of exceptions

And now, May 27, 1930, it is hereby stipulated and agreed by and between respective counsel for plaintiff and defendant in the above-entitled case, that the matter contained in the bill of exceptions heretofore agreed upon by and between said respective counsel as the plaintiff's bill of exceptions in said plaintiff's appeal, and heretofore, on April 23, 1930, by the court allowed, settled, signed, sealed and ordered filed as plaintiff's bill of exceptions, be the defendant's bill of exceptions in defendant's appeal, and it is further agreed that the order hereto annexed may be signed by the court without further notice to either party.

LOUIS E. GRAHAM,
U. S. Attorney,
W. J. AIKEN,
Asst. U. S. Attorney,
Attorneys for the Defendant.
SMITH, SHAW, MCCLAY & SEIFERT,
Attorneys for the Plaintiff.

Order

And now, to wit, May 27, 1930, it is ordered that in pursuance of the foregoing stipulation entered into by and between the
2 respective counsel for plaintiff and defendant, that the matter contained in the bill of exceptions heretofore allowed, settled, signed, sealed and ordered filed as the plaintiff's bill of exceptions, be and hereby is, allowed, settled, signed, sealed and ordered filed as the defendant's bill of exceptions, this order being made and entered within the period in which an appeal may lie from the final judgment entered herein on the 14th day of February, 1930, and within the order of court extending to the defendant time for filing bill of exceptions until May 28, 1930.

Per Curiam,

G.

In United States District Court

Plaintiff's bill of exceptions

Be it remembered that at the trial of this cause in this court, at the regular November term thereof, 1928, holden at the city of Pittsburgh, Pennsylvania, before the Honorable Robert M. Gibson, district judge, on the 21st day of January, 1929, written stipulation waiving jury trial was first filed with the clerk, and the cause was tried to the court without a jury on the said date, the said written stipulation and the proceedings at the trial, subsequent to filing of the same, being as follows:

3 *Stipulation waiving jury trial*

And now, to wit, January 21, 1929, it is stipulated and agreed by the above named plaintiff and by the above respective defendants that a jury trial be waived and that the cases be tried by the court without the interposition of a jury. This stipulation, however, not to affect the rights of any of the parties to appeal, review or other appropriate proceedings in appellate courts.

SMITH, SHAW & MCCLAY,
Attorneys for Plaintiff.
JOHN D. MEYER,
U. S. Attorney.
JOHN A. MCCANN,
Spec. Asst. to U. S. Atty.,
Attorneys for the Respective Defendants.

4 IN UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF PENNSYLVANIA

No. 5761 Law

DIAMOND ALKALI COMPANY, A CORPORATION

vs.

C. G. LEWELLYN, FORMERLY COLLECTOR OF INTERNAL REVENUE FOR THE TWENTY-THIRD DISTRICT OF PENNSYLVANIA

No. 5762 Law

DIAMOND ALKALI COMPANY, A CORPORATION

vs.

D. B. HEINER, COLLECTOR OF INTERNAL REVENUE FOR THE TWENTY-THIRD DISTRICT OF PENNSYLVANIA

And now, to wit, Monday, January 21, 1929, at 10.00 o'clock, a. m., the above entitled cases came on to be heard before Hon. Robert M. Gibson, P. J., at Pittsburgh, Pennsylvania.

Counsel present:

For the plaintiff: Hon. John W. Davis, Montgomery B. Angell, Esq., Marion N. Fisher, Esq., Messrs. Smith, Shaw, McClay & Seifert (by W. A. Seifert, Esq., and Maynard Teall, Esq.).

5 For the defendants: John A. McCann, Esq., Eldon O. Hanson, Esq., special attorneys, Bureau of Internal Revenue; John D. Meyer, Esq., U. S. district attorney.

HARRIET M. COLE,
Official Reporter.
By HARRIET M. COLE,
MARGARET E. ROGAN.

(Counsel for the respective parties file stipulation waiving trial by jury.)

(Mr. Davis presents outline of plaintiff's contention.)

(Mr. McCann presents outline of defendants' contention.)

6–29 [Omitted.]

30 *Testimony of Thomas R. Evans*

Thomas R. Evans, a witness produced on behalf of the plaintiff, having been duly sworn, testified as follows:

Direct examination, Mr. TEALL:

Q. Where do you reside, Mr. Evans?

A. Pittsburgh.

Q. How long have you lived in Pittsburgh?

31 A. All my life.

Q. What is your occupation?

A. I am president of the Diamond Alkali Company.

Q. How long have you been president of the Diamond Alkali Company?

A. For ten years.

Q. Were you connected with it prior to the time you became president?

A. Before I became president, I was vice president and general manager.

Q. State whether or not your connection with the company began at or about the time of its organization?

A. It did. I was instrumental in organizing it, and became its vice president and general manager upon its organization.

Q. What business is this company engaged in?

A. We are engaged in the manufacture of alkali, which consists of soda ash, caustic soda, and baking soda.

32–41 [Omitted.]

42 Q. It appears in the pleadings that have been read into evidence that in the years 1918 and 1920, the Matheson Alkali Works, the Solvay Process Company, the Columbia Chemical Company, and the Michigan Alkali Company were engaged in the manufacture of alkali. Will you state whether in those years, or in any of them, there was any other company, with the exception of those, that were engaged in that business?

Mr. McCann. That is objected to as incompetent, irrelevant, and immaterial, and has nothing to do with any issue in the case.

Mr. Teall. The point of that, I may say frankly to your honor, is in connection with the special assessment point that your honor has considered before, and I assume that objection will probably be sustained.

The Court. Yes. I suggest that you make a general

43 offer to prove by witness thus and so in that connection, and then I can rule on that particular phase, and you can take your exception and your record will probably be in better shape.

Mr. Teall. The plaintiff offers to prove by the witness on the stand that during the years 1918 and 1920, and both of them, at except for this plaintiff, the only persons or corporations engaged, in the United States, in the manufacture of alkali, or in a like or similar trade or business to that of this plaintiff, were the following: The Matheson Alkali Works, the Solvay Process Company, the Columbia Chemical Company, and the Michigan Alkali Company. This in connection with the point of special assessment, which has been raised in the statement of claim.

Mr. McCann. That is objected to as incompetent, irrelevant, and immaterial; and on the further ground that the court is without

power to review actions of the commissioner in determining special assessments.

Mr. TEALL. And we offer at the same time to produce other witnesses to corroborate this witness on the point that I have mentioned, and to prove that the Commissioner of Internal Revenue, in determining the special assessment rate, did not use these corpo-
44 rations, or any of them, as comparatives, and that the average ratio of excess profits tax and war profits tax to income over and above the exemption of $3,000, was, for the corporations I have named, 28 per cent for the year 1918, and less than that for the year 1919.

Mr. MCCANN. The same objection, your honor.

Objection sustained. Exception noted to plaintiff.

45-220 [Omitted.]

221 *Testimony of A. G. Wallerstedt*

A. G. Wallerstedt, a witness produced on behalf of the plaintiff, having been duly sworn, testified as follows:

Direct examination, Mr. TEALL:

Q. You reside where, Mr. Wallerstedt?

A. Pittsburgh.

Q. How long have you lived here?

A. About five years.

Q. What is your occupation?

A. Certified accountant.

Q. Prior to your coming to Pittsburgh, what was your occupation?

A. I was in the service of the Bureau of Internal Revenue, income tax division.

Q. In what capacity?

A. As accountant or auditor.

222 Q. State whether or not you have been one of the advisers and accountant tax counsel of the Diamond Alkali Company in this case, for some time?

A. I have.

Q. For how long?

A. Probably five years.

Q. And during that time have you had occasion to have conferences in the Income Tax Unit with representatives of the Commissioner of Internal Revenue with regard to this case?

A. I have.

Mr. TEALL. The plaintiff offers to prove by the witness on the stand that the abnormalities upon which the commissioner determined, and so declared of record, entitled this corporation to special assessment for the years for which special assessments were allowed were abnormalities of capital and not abnormalities of income. This for the purpose of showing that irrespective of any changes in the income that this court may allow, the plaintiff is still entitled to

special assessment, because the abnormalities continue through all the years.

Mr. McCann. We note an objection, on the ground it is incompetent, irrelevant, and immaterial, and is a direct attempt to go into the question of special assessment, which has already been ruled upon by the court adversely to the plaintiff and that it is an attempt
223 to go into an act which has been performed by the Commissioner of Internal Revenue, pursuant to the discretion confided in him by Congress, under sections 327 and 328 of the revenue act of 1918.

Objection sustained. Exception noted to plaintiff.

(Witness withdrawn.)

Plaintiff rests.

224–321 [Omitted.]

322 *Motions for judgment*

Mr. Teall. The plaintiff presents a motion in writing, and files the motion herewith in each case, for judgment for the plaintiff for the full amount of its claim, under all the evidence.

Mr. McCann. Defendants in cases 5761 and 5762 file written motion for judgment in their favor on the ground that the pleadings and evidence in each case are insufficient to support a verdict for the plaintiff in each case.

The Court. All right, let them be filed.

It is stipulated by counsel, and so ordered by the court, that trial shall be kept open for a period of thirty days from date, for the purpose of permitting counsel on either side to submit request for special findings of fact.

[Testimony closed]

323 [Reporter's certificate to foregoing transcript omitted in printing.]

[Judge's certificate to foregoing transcript omitted in printing.]

324 [Clerk's certificate to foregoing transcript omitted in printing.]

325 *Plaintiff's Exhibit No. 1*

Form 843, Jan., 1922

TREASURY DEPARTMENT,
INTERNAL REVENUE SERVICE,
COMPTROLLER GENERAL, U. S., *January 18, 1922.*

1918

(Execute separate form for each tax period)

CLAIM FOR

[ ] ABATEMENT OF TAX ASSESSED
[ ] CREDIT AGAINST OUTSTANDING ASSESSMENTS
[x] REFUND OF TAXES ILLEGALLY COLLECTED
[ ] REFUND OF AMOUNTS PAID FOR STAMPS

Used in error or excess

NOTICE TO COLLECTOR: Collector must indicate in block above the kind of claim, except in income tax cases.

IMPORTANT: File with collector of Internal Revenue where assessment was made. Not acceptable unless completely filled in.

Date received by administrative unit: Stamp here.

326 COLLECTOR'S NOTATION.—
District----------
Account number----------
Date received ----------
Stamp here.

----------,
Collector of Internal Revenue.

STATE OF PENNSYLVANIA,
County of Allegheny, ss:

Type or print: Diamond Alkali Company.
(Name of taxpayer or purchaser of stamps.)
First National Bank Building.
(Residence—give street and number as well as city or town and State.)
Pittsburgh, Pennsylvania.
(Business address.)

This deponent, being duly sworn according to law, deposes and says that this statement is made on behalf of the taxpayer named,

and that the facts given below with reference to said statement are true and complete:

	Period	Year
From:	Jan. 1,	1918
To:	Dec. 31,	1918

1. Business in which engaged: Alkali products.
2. Character of assessment or tax (state for or upon what the tax was assessed or the stamps affixed); Income and excess profits.
3. Amount of assessment or stamps purchased ..... $.....
327 4. Reduction of tax liability requested (income and profits tax) $1,215,615.14
5. Amount to be abated ..... $.....
6. Amount to be refunded (or such greater amount as is legally refundable) with interest $1,333,354.22
7. Dates of payment (see collector's receipts or indorsements of canceled checks). 11/15/27.
(If statement covers income-tax liability, items 8–11, inclusive, must be answered.)
8. District in which return (if any) was filed. 23rd Pennsylvania.
9. District in which unpaid assessment appears .....
10. Amount of overpayment claimed as credit ..... $.....
11. Unpaid assessment against which credit is asked; period from ..... to ..... $.....

Deponent verily believes that this application should be allowed for the following reasons:

1. The taxpayer is entitled to deduct from its gross income for the year 1918 the amount of $876,366.71, representing exhaustion, wear, and tear, suffered by it on property used in its trade or business, and deducted by the taxpayer on its books and in its income-tax return, for the calendar year 1918.

2. The taxpayer is entitled to deduct from its gross income the amount of $1,245,448.21, representing amortization sustained by it for the calendar year 1918, on facilities used by it and which contributed to the prosecution of the recent war with Germany.

328 3. The commissioner's redetermination made after March 3, 1924, of the amortization deductible by the taxpayer on its said war-time facilities was illegal, void, and of no effect. (Continued on attached sheet.)

(Attach additional sheets if necessary.)

4. The Commissioner of Internal Revenue erroneously and illegally reduced the taxpayer's invested capital by prorating an alleged additional tax for 1917 in the amount of $574,372.90, whereas the final determination of the commissioner resulted in an additional tax of $269,451.93.

5. The Commissioner of Internal Revenue properly determined the taxpayer's excess and war profits tax under the provisions of section 327 of the revenue act of 1918 in accordance with a petition filed by it. The commissioner applied a percentage of 54.54+ against the net income of $3,821,143.63 as determined by him and arrived at an excess and war profits tax of $2,084,324.26. The commissioner's rate of 54.54+ was determined as follows:

"Your profits tax is based upon a comparison with a group of representative concerns, which in the aggregate, may be said to be engaged in a like or similar trade or business to that of your company."

The taxpayer does not know what comparatives were used and the commissioner refused to make them known to it. Under the Osterlein decision of the Supreme Court of the United States the
329 comparatives used by the commissioner should be made known.

The taxpayer submitted the names of all the companies in the United States engaged in a like or similar business but it is not known whether the commissioner used any of these companies as comparatives. The comparatives submitted by taxpayer, if used, would result in a percentage considerably less than 54.54+. It is therefore submitted that the excess and war profits tax for this year should be recomputed under sections 327 and 328 and the proper comparatives used.

6. The Commissioner of Internal Revenue erroneously and illegally assessed and collected an additional tax of $1,215,615.14, together with interest thereon, in the amount of $117,739.08, because the assessment and/or collection of said amount of tax or any tax was barred by the Statute of Limitations, and any liability extinguished. Therefore both the assessment and the collection of the said additional tax was illegal, void, and without authority of law.

7. The above amount of $1,333,354.22 is made up as follows:

Tax assessed and collected on November 15, 1927	$1,215,615.14
Interest assessed and collected on Nov. 15, 1927	117,739.08
Total	1,333,354.22

Payment of this tax and interest was made under protest
330 and duress and to avoid penalties, interest, distraints, seizures, etc., threatened by the collector.

(Signed) DIAMOND ALKALI COMPANY,
By W. E. JONES, (sgd.)
Treasurer.

Sworn to and subscribed before me this 5th day of December, 1927.

[SEAL.] WILLIAM C. MAHAN, (sgd.)
Notary Public.
(Title.)

My commission expires Jan. 20, 1930.

(This affidavit may be sworn to before a deputy collector of internal revenue or revenue agent without charge.)

331–353 [Omitted.]

354 *Plaintiff's Exhibit No. 4*

Form NP-1

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, Mar. 19, 1927.

Address reply to Commissioner of Internal Revenue and refer to
IT:E:SM
AWL-A-31086
B-31087
C-31088

DIAMOND ALKALI COMPANY,
511 Wood Street, Pittsburgh, Pennsylvania.

SIRS: An audit of your income and profits tax returns for the years 1918, 1919, and 1920 has resulted in the determination of a deficiency in tax of $1,755,205.93, as shown in the attached statement.

355 You are granted 30 days from the date of this letter within which to present a protest against the deficiency proposed herein. The protest and any additional statements of facts must be executed in triplicate, under oath, and contain the following information:

(a) The name and address of the taxpayer (in the case of an individual the residence, and in the case of a corporation the principal office or place of business); (b) in the case of a corporation the name of the State of incorporation; (c) the designation by date and symbol of the letter advising of the proposed deficiency with respect to which the protest is made; (d) the designation of the year or years involved and a statement of the amount of tax in dispute for each year; (e) an itemized schedule of the findings to which the taxpayer takes exception; (f) a summary statement of the grounds upon which the taxpayer relies in connection with each exception; and (g) in case the taxpayer desires a hearing, a statement to that effect.

If a protest is filed, any additional evidence or briefs of argument submitted will be given careful consideration, and if the commissioner finally determines that there is a deficiency, you will be advised thereof by registered mail in accordance with the provisions of section 274 of the revenue act of 1926. Should you not agree to the deficiency as finally determined by the commissioner, you will be allowed 60 days from the date of mailing of the registered letter (not counting Sunday as the sixtieth day) in which to file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

If you acquiesce in the proposed deficiency as shown in this letter and the accompanying statement, you are requested to execute a waiver of your right to file a petition with the United States Board

of Tax Appeals on the inclosed Form A, and forward it to
356 the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:E:SM-AWL-A-31086-B-31087-C-31088. In the event that you acquiesce in a part of such deficiency, the waiver should be executed with respect to the items to which you agree.

Respectfully,

C. R. NASH,
Assistant to the Commissioner.

Inclosures:
Statement
Form A.

STATEMENT

IT:E:SM
AWL-A-31086
B-31087
C-31088

In re: Diamond Alkali Company, 511 Wood Street, Pittsburgh, Pennsylvania.

Year:	Deficiency in tax
1918	$1,485,420.75
1919	191,181.09
1920	78,604.09
Total	1,755,205.93

You are advised that after careful consideration and review, your application under the provisions of section 327 for assessment of your profits tax as prescribed by section 328 of the revenue act of 1918, for the year 1918, has been allowed. Your profits tax is based upon a comparison with a group of representative concerns which in the aggregate may be said to be engaged in a like or similar trade or business to that of your company.

357 The result of the audit under the above provisions is as follows:

1918

Profits tax, section 328			$2,390,921.54
Net income as readjusted		$3,821,143.63	
Less:			
Interest on United States obligations not exempt	$17,819.46		
Profits tax, section 328	2,390,921.54		
Exemption	2,000.00		
		2,410,741.00	
Balance taxable at 12%		$1,410,402.63	169,248.32
Total tax assessable			$2,560,169.86
Previously assessed, account #403453			1,074,749.11
Deficiency			$1,485,420.75

1919 and 1920

Your application under the provisions of section 327 for assessment of your profits tax as prescribed by section 328 of the revenue act of 1918, for the years 1919 and 1920, has been denied inasmuch as the audit disclosed no exceptional hardship evidenced by gross disproportion between the tax computed without benefit of the above section and the tax computed by reference to the representative corporations specified in section 328.

The tax liability for these years has been changed by reason of the change in the tax liability for the preceding year 1918.

Computation of the tax liability for the years 1919 and 1920 follows:

358

1919

Net income

Consolidated net income as disclosed by office letter dated December 23, 1925		$2,721,689.54
As corrected		2,708,248.07
Net adjustment		$13,441.47
Unallowable deductions and additional income: (a) Amortization		$16,378.37
Nontaxable income and additional deductions:		
(b) Plant and equipment abandoned	$19,847.97	
(c) Depreciation	9,971.87	
Total		29,819.84
Net adjustment as above		$13,441.47

Explanation of items changed

(a) See explanation under Schedule 1 (b).		
Amortization allowed 1919 Schedule 1 (b)		$18,202.10
14.38% of $369,022.30 (see Schedule 1 (b))		53,065.41
Total amortization allowed 1919		$71,267.51
Amount shown in office letter dated December 23, 1925		87,645.88
Excessive amortization disallowed		$16,378.37
(b) See explanation under Schedule 1 (c).		
(c) See explanation under Schedule 1 (a).		
Plant and equipment December 31, 1917 (Schedule 1)		$4,677,006.70
359 Additions 1918		1,519,450.75
Total		$6,196,457.45
Less:		
Property abandoned 1918	$79,753.15	
Amortization allowed 1918	315,956.89	
		395,710.07
Plant and equipment December 31, 1918		$5,800,747.41
Cost upon which amortization is allowed, 1917–1918		1,776,755.40
Balance to be depreciated		$4,023,992.01
Depreciation allowed, $4,023,992.01 at 10.4%		$418,495.17
Additions 1919	$291,002.28	
Cost upon which amortization is allowed 1919	$86,735.02	

Property abandoned 1919	$41,093.62	
		$127,828.64
Balance to be depreciated, ½ year	$163,173.64	$8,485.03
Cost upon which amortization is allowed 1917–1918	$1,776,755.40	
Amortization allowed 1919	71,267.51	
Balance to be depreciated effective 9 months	$1,705,487.89	133,028.06
(The date of cessation of operation as a war facility was March 31, 1919.)		
Total depreciation allowed		$560,008.26
Amount allowed in office letter dated December 23, 1925		550,036.39
Additional depreciation allowed		$9,971.87

360 *Consolidated invested capital 1919*

As shown by office letter dated December 23, 1925		$6,450,683.71
As corrected		6,656,664.49
Net increase as explained below		$205,980.78
Increases:		
(a) Amortization disallowed 1918	$65,209.53	
(b) Reserve for depreciation	50,332.20	
(c) Additional income tax prior years	160,192.20	
(d) Intercompany loss on sale of locomotive	10,000.00	
Total increase		$285,733.93
Decrease:		
(e) Cost of plant and equipment abandoned 1918		79,753.15
Net increase as above		$205,980.78

Explanation of items changed

(a) The amortization disallowed as a deduction from income as shown in Schedule 1 (b) is here restored to invested capital.

(b) Reserve for depreciation.

Excessive depreciation disallowed 1918, shown in Schedule 1 (a)	$22,386.46
Depreciation on plant and equipment abandoned during 1918, credited to reserve	27,945.74
Total addition to invested capital	$50,332.20

(c) Additional income tax for 1917 of Diamond Alkali Company, shown by office letter dated December 23, 1925 $574,372.90

361 As adjusted 487,440.69

Addition to invested capital	$86,932.21
Income tax, 1918 (section 328), $2,560,169.86.	
Proration, $2,560,169.86 x .42260273	$1,081,934.77
Amount shown in office letter dated December 23, 1925	1,155,194.76
Addition to invested capital	$73,259.99
Total addition for adjustment in 1917 and 1918 taxes	$160,192.20

(d) See explanation under Schedule 2(a).

(e) The cost of plant and equipment abandoned during 1918 as shown in brief dated May 14, 1926, is here eliminated from invested capital.

Proof of invested capital

Capital stock	$2,613,500.00
Surplus	5,317,856.15
Reserves	
Premium on sale of capital stock	392,996.34
Capital surplus (Harbor Land Company)	20,000.00
	464.36
Total, corrected balance sheet beginning of year	$8,344,816.85

Additions:		
Sale of capital stock		$1,369.86
Intercompany loss, 1917		10,000.00
Total		$8,356,186.71
Reductions:		
Income tax, 1918		$1,081,934.77
Additional income tax, prior year	493,846.56	
362 Dividends	121,647.94	
Inadmissibles	2,092.95	
Total, deduct from above		1,699,522.22
As shown in Schedule #7		$6,656,664.49

Computation of excess-profits credits

Consolidated net income, taxable year (Schedule 6)	$2,708,248.07
Consolidated invested capital, taxable year (Schedule 7)	$6,656,664.49

Excess-profits credit

8% of invested capital for taxable year	$532,533.16
Exemption	3,000.00
Excess-profits credit	$535,533.16

Computation of total tax (1919)

Excess-profits tax		
Net income for taxable year	$2,708,248.07	
Less:		
Excess-profits credit	535,533.16	
Balance	$2,172,714.91	
Taxable at 20%	$795,799.74	$159,159.95
Taxable at 40%	$1,376,915.17	550,766.07
		$709,926.02
Income tax		
Net income for taxable year	$2,708,248.07	
363 Less:		
Interest on obligations of the United States, not exempt	$69,981.11	
Excess-profits tax	709,926.02	
Exemption	2,000.00	
	781,907.13	
Taxable at 10%	$1,926,340.94	192,634.09
Total, excess-profits and income taxes		$902,560.11
Previously assessed, Account #401503		711,379.02
Additional tax to be assessed		$191,181.09

1920

Net income

Net income as disclosed by office letter dated December 23, 1925	$1,475,586.11
As corrected	1,529,710.37
Net adjustment	$54,124.26
Unallowable deductions and additional income:	
(a) Depreciation	$82,568.30

Nontaxable income and additional deductions:			
(b) Plant and equipment abandoned			$28,444.04
Net adjustment as above			$54,124.26

364 Explanation of items changed

(a) See explanation under Schedule 1 (a).

Plant equipment December 31, 1918, Schedule 6 (c)			$5,800,747.41
Additions 1919			291,002.28
Total			$6,091,749.69
Less:			
Amortization allowed 1919	$71,267.51		
Property abandoned	41,093.62		
			112,361.13
Plant and equipment December 31, 1919			$5,979,388.56
Depreciation allowed: $5,979,388.56 at 10.4%			$621,856.41
Additions:			
1920	$591,369.58		
Property abandoned 1920	66,390.69		
Balance to be depreciated effective ½ year	$524,978.89		27,298.90
Total depreciation allowed			$649,155.31
Depreciation allowed in office letter dated December 23, 1925	$656,690.55		
Depreciation allowed by examiner:			
General plant	$708,360.83		
Caustic soda department	75,033.06		
Total	$783,393.89		
365 Amount shown by office letter dated December 23, 1925	708,360.83	75,033.06	731,723.61
Excessive depreciation disallowed			$82,568.30

(b) See explanation under Schedule 1 (c).

Consolidated invested capital 1930

As shown by office letter dated December 23, 1925			$6,692,559.87
As corrected			6,992,170.97
Net increase as explained below			$299,611.10
Increases:			
(a) Amortization disallowed 1918 and 1919	$81,587.90		
(b) Reserve for depreciation	61,605.98		
(c) Additional income tax prior years	260,281.20		
(d) Intercompany loss on sale of locomotive	10,000.00		
(e) Income tax 1919	6,982.79		
Total increase			$420,457.87
Decrease:			
(f) Cost of plant and equipment abandoned			120,846.77
Net increase as above			$299,611.10

Explanation of items changed

(a) Amortization.

Amortization disallowed 1918 Schedule 1 (b)	$65,209.53
Amortization disallowed 1919 Schedule 6 (a)	16,378.37
Total addition to invested capital	$81,587.90

366 (b) Reserve for depreciation forwarded from Schedule 7 (b)		$50,332.20
Depreciation on assets abandoned during 1919		21,245.65
Total		$71,577.85
Less:		
Additional depreciation allowed 1919		$9,971.87
Net addition to invested capital		$61,605.98
(c) Additional income tax prior years.		
Forwarded from Schedule 7 (c)		$86,932.21
Additional income tax 1918 as adjusted	$1,485,420.75	
Amount shown by office letter dated December 23, 1925	1,658,769.74	
		173,348.99
Addition to invested capital		$260,281.20
(d) See explanation under Schedule 2 (a).		
(e) Income tax 1919	$902,560.11	
Proration ($902,560.11 × .421448)		$380,382.15
Amount shown in office letter dated December 23, 1925		387,364.94
Addition to invested capital		$6,982.79
(f) Cost of plant and equipment abandoned.		
Forwarded from Schedule 7 (e)		$79,753.15
Cost of assets abandoned 1919		41,093.62
Total reduction of invested capital		$120,846.77

Proof of invested capital

Capital stock		$2,623,500.00
Surplus		6,352,421.70
367 Reserves		420,751.44
Premium on sale of capital stock		20,000.00
Capital surplus (Harbor Land Company)		464.36
Surplus transferred by Armstrong Fuel Company		11,434.83
Total, corrected balance sheet beginning of year		$9,428,572.33
Additions:		
Sale of capital stock		$43,278.69
Intercompany loss 1920		10,000.00
Total		$9,481,851.02
Reductions:		
Income tax 1919	$380,382.15	
Additional income tax prior years	1,979,267.31	
Dividends	123,877.05	
Inadmissibles	6,153.54	
Total, deduct from above	$2,489,680.05	2,489,680.05
As shown in Schedule #12		$6,992,170.97

Computation of Tax, 1920 Rates
Excess Profits Tax

Net income, Schedule 11	$1,529,710.37
Invested capital, Schedule 12	$6,992,170.97
8% of invested capital	$559,373.68
Plus: Exemption	3,000.00
Total credit	$562,373.68

368	Income	Credit	Taxable	Rate	Tax
20% Balance	$1,398,434.19 131,276.18	$562,373.68	$836,060.51 131,276.18	20% 40%	$167,212.10 52,510.47
Totals	$1,529,710.37	$562,373.68	$967,336.69		$219,722.57

Income Tax

Net income taxable year		$1,529,710.37	
Less:			
Interest on United States obligations not exempt	$80,253.71		
Excess profits tax	219,722.57		
Exemption	2,000.00		
		301,976.28	
Balance taxable at 10%		$1,227,734.09	122,773.41
Total income and excess profits tax			$342,495.98
Previously assessed, account #404260			263,891.89
Additional to be assessed			$78,604.09

In accordance with the above conclusions, your two claims for refund, each for the amount of $45,000.00, for the year 1918; your claim for the refund of $45,000.00 for the year 1919 and your claim for the refund of $45,000.00 for the year 1920, will be rejected in full.

The collector of internal revenue for your district will be officially notified of the rejection at the expiration of thirty days from the date of this letter.

Upon receipt of notice and demand from that official payment should be made to his office in accordance with the conditions of his notice.

369 A copy of this letter has been furnished your authorized representatives, Messrs. Reed, Smith, and McClay, Union Arcade Building, Pittsburgh, Pennsylvania.

In re: Diamond Alkali Company,
Pittsburgh, Pennsylvania.

IT:E:SM Form A
AWL—A–31086
B–31087
C–31088

Waiver of right to file a petition with the U. S. Board of Tax Appeals

Mar. 19, 1927

The undersigned taxpayer hereby waives the right to file a petition with the U. S. Board of Tax Appeals under section 274 (a) of the revenue act of 1926 and consents to the assessment and collection of a deficiency in tax for the years 1918, 1919, and 1920 aggregating $1,755,205.93.

(Corporate seal to be affixed; if no seal, so state.)

(Name)

(Address)

Date---------- By ----------

NOTE.—This waiver does not extend the statute of limitations for refund or assessment of tax, and is not an agreement as provided under section 1106 of the revenue act of 1926.

370 This copy to be retained by taxpayer.

In re: Diamond Alkali Company,
Pittsburgh, Pennsylvania.

IT: E: SM. Form A
AWL—A–31086
B–31087
C–31088

Waiver of right to file a petition with the U. S. Board of Tax Appeals

Mar. 19, 1927

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(Corporate seal to be affixed; if no seal, so state.)

(Name)

(Address)

Date---------- By ----------

NOTE.—This waiver does not extend the statute of limitations for refund or assessment of tax, and is not an agreement as provided under section 1106 of the revenue act of 1926.

371 *Notice*

Appeals should be adressed to the United States Board of Tax Appeals, Earle Building, Washington, D. C., in accordance with the rules of practice established by that board.

The United States Board of Tax Appeals is in no way connected with the Bureau of Internal Revenue or the Treasury Department. Under no circumstances should a petition on appeal be forwarded to the Commissioner or the Collector of Internal Revenue. If you decide to initiate a proceeding before the board, your petition, proceedings, and proofs in the proceedings must be in accordance with the rules of practice of the board, with section 900 of the revenue act of 1924 and section 1000 of the revenue act of 1926. Under the statute and the rulings of the board a petition (together with a filing fee of $10.00) must be received and filed with the board within sixty days from the date of mailing of the attached notice (not counting Sunday as the sixtieth day).

372 *Plaintiff's exhibit No. 5*

Form N P–2

TREASURY DEPARTMENT

Washington

OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Jul 11, 1927.

IT:CA:SM:60D
EMB—A–31086.
B–31087.
C–31088.

DIAMOND ALKALI COMPANY,
511 Wood Street, Pittsburgh, Pennsylvania.

SIRS: An audit of your income and profits tax returns for the years 1918, 1919, and 1920 has resulted in the determination of deficiencies in tax of $1,215,615.14 for 1918 and $60,769.03 for 1920 and an overassessment of $1,467.64 for 1919, as shown in the attached statement.

In accordance with the provisions of section 274 of the revenue act of 1926 you are allowed 60 days from the date of mailing of this letter within which to file a petition for the redetermination of this deficiency. Any such petition must be addressed to the United
373 States Board of Tax Appeals, Earle Building, Washington, D. C., and must be mailed in time to reach the board within the 60-day period, not counting Sunday as the sixtieth day.

Where a taxpayer has been given an opportunity to file a petition with the United States Board of Tax Appeals and has not done so within the 60 days prescribed and an assessment has been made,

or where a taxpayer has filed a petition and an assessment in accordance with the final decision on such petition has been made, the unpaid amount of the assessment must be paid upon notice and demand from the Collector of Internal Revenue. No claim for abatement can be entertained.

If you acquiesce in this determination and do not desire to file a petition with the United States Board of Tax Appeals, you are requested to execute a waiver of your right to file a petition with the United States Board of Tax Appeals on the inclosed Form A, and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention IT:CA:SM:60D:EMB–A–31086, B–31087, C–31088. In the event that you acquiesce in a part of the determination, the waiver should be executed with respect to the items to which you agree.

Respectfully,

D. H. BLAIR,
Commissioner.
By C. R. NASH,
Assistant to the Commissioner.

374 Inclosures:
Statement.
Form A.

STATEMENT

IT:CA:SM:60D.
EMB—A–31086.
B–31087.
C–31088.

In re: Diamond Alkali Company, 511 Wood Street, Pittsburgh Pennsylvania

Year	Deficiency in tax	Overassessment
1918	$1,215,615.14	
1919		$1,467.64
1920	60,769.03	
Totals	$1,276,384.17	$1,467.64

Reference is made to your protests executed April 12, 1927, and May 4, 1927, against the determination of net income and the result of the allowance of your application for assessment of your profits tax for the year 1918 under the provisions of section 328 of the revenue act of 1918 and against the denial of your application for the years 1919 and 1920 as set forth in bureau letter dated March 19, 1927.

After a careful review of your protests and of all the information submitted in support of your contentions at a conference held
375 on May 4, 1927, you are advised that the bureau holds the following relative to the statutory points protested:

1. Disallowance of amounts expended for compromise and settlement of divers law suits, instituted or threatened to be instituted, as deductions from income for the years 1918, 1919, and 1920. No loss has been suffered until the properties are disposed of at a price less than the amount paid.

2. Greater allowance for amortization in the years 1918 and 1919. The evidence submitted does not warrant any further increase in the amount of amortization previously allowed.

3. Depreciation and obsolescence. After a careful consideration of the entire information presented, the depreciation allowance of a composite rate of 10.4% for each of the years 1918, 1919, and 1920 is sustained.

4. Relative to the findings under the provisions of section 328 of the revenue act of 1918 the bureau recommends the following:

1918

That your profits tax determined under section 328 of the revenue act of 1918 be recomputed under these provisions.

1919

That your application under the provisions of section 328 of
376 the revenue act of 1918 has been allowed. Your profits tax is based upon a comparison with a group of representative concerns, which in the aggregate may be said to be engaged in a like or similar trade or business to that of your company.

1920

That your application for assessment of your profits tax under the provisions of section 328 was properly denied because comparison has been made with representative corporations as nearly as may be similarly circumstanced as contemplated under section 328 of the revenue act of 1918, and your profits tax computed under the provisions of section 301 of the revenue act of 1918 is not disproportionate to the profits tax paid by such representative concerns. Due to changes in your tax liability for 1918 and 1919, a recomputation of invested capital and tax liability for this year has been made.

The result of the audit under the provisions of section 328 for the years 1918 and 1919 and under the provisions of section 301 for 1920 is as follows:

1918

Net income as shown by bureau letter dated March 19, 1927		$3,821,143.63
Profits tax, section 328		$2,084,324.26
Net income	$3,821,143.63	

377	Less:		
	Interest on United States obligations not exempt	$17,819.46	
	Profits tax	2,084,324.26	
	Exemption	2,000.00	
		2,104,143.72	
	Balance taxable at 12%	$1,716,999.91	
	Tax at 12%		206,039.99
	Correct tax liability		$2,290,364.25
	Previously assessed, original tax, account #403453		1,074,749.11
	Deficiency in tax		$1,215,615.14

1919

	Net income as shown by bureau letter dated March 19, 1927		$2,708,248.07
	Profits tax, section 328		$495,871.87
	Net income	$2,708,248.07	
	Less:		
	Interest on U. S. obligations not exempt	$69,981.11	
	Profits tax	495,871.87	
	Exemption	2,000.00	
		567,852.99	
	Balance taxable at 10%	$2,140,395.09	
378	Tax at 10%		214,039.51
	Correct tax liability		$709,911.38
	Previously assessed, original tax, account No. 401503		$711,379.02
	Correct tax liability		709,911.38
	Overassessment		$1,467.64

1920

	Net income as shown by bureau letter dated March 19, 1927		$1,529,710.37
	Invested capital as shown by bureau letter dated March 19, 1927		$6,992,170.97
	Plus:		
	(a) Adjustment for 1918 tax liability		269,805.61
	(b) Adjustment for 1919 tax liability		84,064.49
	Adjusted invested capital		$7,346,041.07

Explanation of items changed

(a)	Additional tax for 1918:		
	Additional tax for 1918 as adjusted		$1,215,615.14
	Amount shown by Bureau letter dated December 23, 1925		1,658,769.74
379	Correct addition to invested capital		$443,154.60
	Less addition as shown by bureau letter date March 19, 1927		173,348.99
	Additional to be restored		$269,805.61
(b)	Tax liability for 1919, $703,094.23:		
	Proration ($703,094.23x.421448)		$296,317.66
	Amount shown by bureau letter dated December 23, 1925		387,364.94
	Correct addition to invested capital		$91,047.28
	Less addition as shown by bureau letter dated March 19, 1927		6,982.79
	Additional to be restored		$84,064.49

Excess profits credit

8% of invested capital, $7,346,041.07	$587,683.29
Plus exemption	3,000.00
Total credit	$590,683.29

380 % of Capital	Income	Credit	Balance	Rate	Tax
20%	$1,469,203.21	$590,683.29	$878,524.92	20%	$175,704.98
Balance	60,502.16		60,502.16	40%	24,200.86
Totals	$1,529,710.37	$590,683.29	$939,027.08		$199,905.84

Total profits tax		$199,905.84
Net income	$1,529,710.37	
Less:		
Interest on U. S. obligations not exempt	880,253.71	
Profits tax	199,905.84	
Exemption	2,000.00	
	282,159.55	
Balance taxable at 10%	$1,247,550.82	
Tax at 10%		124,755.08
Correct tax liability		$324,660.92
Previously assessed, original tax, account #404260		263,891.89
Deficiency in tax		$60,769.03

In accordance with the above conclusions your two claims for the refund of $45,000.00 each, covering the year 1918, will be rejected in full. Your claim for the refund of $45,000.00, covering the year 1919, will be rejected for $43,532.36, and your claim for the refund of $45,000.00, covering the year 1920, will be rejected in full.

381 The collector of internal revenue for your district will be officially notified of the rejections.

The overassessment shown above will be made the subject of a certificate of overassessment which will reach you in due course through the office of the collector of internal revenue for your district and will be applied by that official in accordance with section 284 (a) of the revenue act of 1926.

A copy of this communication has been furnished your authorized representatives, Messrs. Reed, Smith, and McClay, Union Arcade Building, Pittsburgh, Pennsylvania.

Form A

In re Diamond Alkali Company, Pittsburgh, Pennsylvania.

WAIVER OF RIGHT TO FILE A PETITION WITH THE UNITED STATES BOARD OF TAX APPEALS

IT:CA:SM:60D
EMB–A–31086
B–31087
C–31088

JUL 11, 1927.

The undersigned taxpayer hereby waives the right to file a petition with the United States Board of Tax Appeals under section 274 (a) of the revenue act of 1926, and consents to the assess-
382 ment and collection of a deficiency in tax for the years 1918 and 1920 aggregating $1,276,384.17.

(Corporate seal to be affixed; if no seal, so state.)

Taxpayer.

Address.

By ---

NOTE.—This waiver does not extend the statute of limitations for refund or assessment of tax, and is not an agreement as provided under section 1106 of the revenue act of 1926, but its execution and filing at the address shown in the accompanying letter will expedite the adjustment of your income tax liability as indicated above.

Form A

In re Diamond Alkali Company, Pittsburgh, Pennsylvania.

WAIVER OF RIGHT TO FILE A PETITION WITH THE UNITED STATES BOARD OF TAX APPEALS

IT:CA:SM:60D
EMB–A–31086
B–31087
C–31088

JUL 11, 1927.

The undersigned taxpayer hereby waives the right to file a
383 petition with the United States Board of Tax Appeals under section 274 (a) of the revenue act of 1926, and consents to the

assessment and collection of a deficinecy in tax for the years 1918 and 1920 aggregating $1,276,384.17.

(Corporate seal to be affixed; if no seal, so state.)

Taxpayer.

Address.

By ---

This copy to be retained by taxpayer.

rgh–l

NOTE.—This waiver does not extend the statute of limitations for refund or assessment of tax, and is not an agreement as provided under section 1106 of the revenue act of 1926, but its execution and filing at the address shown in the accompanying letter will expedite the adjustment of your income tax liability as indicated above.

384–575 [Omitted.]

576 *Defendants' Exhibit Z*

UNITED STATES OF AMERICA,
TREASURY DEPARTMENT,
Washington, December 28, 1928.

Pursuant to section 882 of the Revised Statutes, I hereby certify that the annexed is a true copy of 30-day letter dated December 23, 1925 (with statement and schedules attached), showing an additional tax of $1,658,769.74 for 1918, to Diamond Alkali Company, Pittsburgh, Pennsylvania, from C. R. Nash, assistant to the commissioner, the original of which are on file in this department.

In witness whereof I have hereunto set my hand, and caused the seal of the Treasury Department to be affixed, on the day and year first above written.

By direction of the Secretary:

[SEAL] F. A. BIRGFELD.
Chief Clerk, Treasury Department.

F. WWB EOH FFT CMC TRM
r

577

Mailed
DEC. 23, 1925.

IT:CR:G–1
CWZ

DIAMOND ALKALI COMPANY,
511 Wood Street, Pittsburgh, Pennsylvania.

SIRS: Reference is made to the request contained in your undated application that your profits tax for the year 1918 be computed under the provisions of section 328 of the revenue act of 1918.

Before consideration can be given your application for special relief there must be a final determination of your tax liability computed on the basis of statutory invested capital.

You are granted thirty days from the date of this letter within which to present a protest, supported by additional evidence or brief, against the determination of your net income and statutory invested capital as shown in the attached statement and accompanying schedules. Upon request submitted within the period mentioned, you will also be granted a hearing in the bureau with reference to the matter.

A request for a hearing should contain (a) the name and address of the taxpayer; (b) in the case of a corporation, the name of the State of incorporation; (c) a designation by date and symbol of the notice or notices with respect to which the hearing is desired;
578 (d) a designation of the year or years involved and a statement of the amount of tax in dispute for each year; (e) an itemized schedule of the findings of the unit to which the taxpayer takes exception; and (f) a summary statement of the grounds upon which the taxpayer relies in connection with each exception.

If no protest is received within the time specified above, it will be considered that you do not desire to protest to the unit against the computation of net income and statutory invested capital as outlined in the attached schedules, and the unit will proceed to the consideration of your request for special relief under the section of the act referred to above.

Respectfully,

C. R. NASH,
Assistant to the Commissioner.

IT:CR:G-1
CWZ

Statement of Returns Examined and Resulting Tax Liability

RETURNS EXAMINED

Company	Year	Form	Date filed
Diamond Alkali Company	1918	1120	June 16, 1919

TAX LIABILITY

	Year	Additional tax
Diamond Alkali Company	1918	$1,658,769.74

The following named companies have been ruled affiliated in a class A and B relationship for the year 1918:
579 Diamond Alkali Company, parent.
Fairport, Painesville & Eastern R. R. Company.
Armstrong Fuel Company.
Harbor Land Company.
Sunshine Soda Company.

Waivers, which will expire December 31, 1926, except as extended by the provisions of section 277 (b) of the revenue act of 1924, are on file for the year 1918.

Due consideration has been given to the statements contained in your claim for refund of $45,000 for the year 1918, filed March 11, 1924.

The revenue agent's report dated July 7, 1922, has been made the basis of this examination.

In the event a protest is made to the adjustments set out herein and a brief filed in which there appear material differences form the facts as shown in the revenue agent's report on which this audit is based, it will be necessary for the bureau to refer your brief to the internal revenue agent in charge for examination and recommendation before a conference can be granted or further action taken thereon by the bureau.

580 *Year ended December 31, 1918—Schedule 1—Net income*

Consolidated net income as disclosed by revenue agent's report dated July 31, 1922		$2,476,658.87
As corrected		3,785,355.05
Net additions		1,308,696.18
Additions:		
(a) Amortization	$744,260.79	
(b) Depreciation	416,717.70	
(c) Obsolescence	150,279.59	
Total additions		1,341,258.08
Deduction:		
(d) Miscellaneous revenue reserve		32,561.90
Net additions as above		1,308,696.18

EXPLANATION OF ITEMS CHANGED

(a) Income has been adjusted on account of amortization determined as follows:

	1917-1918	1919	Total
Cost on which amortization is allowed	$1,776,755.40	$86,735.02	$1,863,490.42
Amortization recommended	446,283.67	22,528.63	468,812.30

Amortization allowed, computed as provided in Article 18b (a) Regulations 62:

Net income before adjustment for amortization 1918	85,409	$4,174,584.73
581 Net income before adjustment for amortization Jan., Feb., and Mar., 1919	14.591	713,386.03
	100%	$4,867,970.76
Amortization allowed 1918, 85.409% 446,283.67=		381,166.42
Amount allowed by examiner		1,155,427.21
Excessive amortization disallowed		774,260.79

(b) Depreciation has been adjusted using the same percentage based on cost of depreciable property as that deducted and allowed for the year 1917 and shown by the examiner to be 10.4%.

Plant & equipment as at December 31, 1918, shown by the examiner		$5,180,384.87
Add:		
Profit on sale of dock restored		6,426.45
Amortization deducted by examiner		1,072,555.10
Total		$6,259,366.42
Less:		
Miscellaneous revenue reserves claimed as credits to plant account (1916, 1917, and 1918)		62,908.97
Plant & equipment as at December 31, 1918, before adjustment for amortization		$6,196,457.45
Less costs upon which amortization is computed		1,776,755.40
Balance to be depreciated		$4,419,702.05
582 Depreciation allowed, 10.4% of $4,419,702.05		459,649.01
Depreciation deducted on return		876,366.71
Excessive depreciation disallowed		$416,717.70

(c) It is noted that the examiner in computing obsolescence has taken into consideration an allowance for amortization on some of the assets. Inasmuch as this office has revised the basis for the allowance of amortization, and on account of the large amount of repairs charged to expense, the entire deduction for obsolescence has been determined. The high rate of depreciation allowed (10.4%) is considered sufficient to take care of all obsolescence sustained.

(d) See explanation under Schedule 1 (b) of separate communication covering the years 1916, 1919, and 1920.

Schedule 2—Consolidated invested capital

As shown by revenue agent's report dated July 31, 1922		$6,117,003.37
As corrected		4,729,176.15
Net decrease as explained below		1,387,827.22
Increases:		
(a) Additional income tax, 1916	386.66	
(b) Profit on sale of dock, 1917 (R. R. Co.)	6,426.45	
Total increase		6,813.11
Decreases:		
(c) Income tax 1917 prorated	$79,396.26	
583 (d) Miscellaneous Revenue Reserve	30,244.07	
(e) Loss on sale of locomotive 1917 (Diamond	10,000.00	
(f) Paid in surplus (contracts)	1,275,000.00	
Total decrease		1,394,640.33
Net decrease as above		$1,387,827.22

Explanation of items changed

(a) Invested capital has been increased on account of additional income tax due for the year 1916.

Diamond Alkali Company, additional income tax due 1916	$6,328.91
Amount shown by examiner	6,715.57
Addition to invested capital	$386.66

(b) See explanation under Schedule 4 (a) of separate communication covering the year 1919.

(c) Invested capital has been reduced on account of income tax for 1917, prorated from the date due and payable.

Diamond Alkali Company	$1,183,278.38
Armstrong Fuel Company	17,842.85
Fairport, Painesville and Eastern R. R. Company	1,755.97
Total	$1,202,877.20
$1,202,877.20 effective 200 days	$659,110.79
Amount shown by examiner	579,714.53
Reduction of invested capital	79,396.26

584 (d) See explanation under Schedule 4 (g) of Separate communication covering the year 1919.

(e) See explanation under Schedule 4 (h) of separate communication covering the year 1919.

(f) See explanation under Schedule 4 (i) of separate communication covering the year 1919.

Schedule 3—Proof of invested capital

Capital stock		$2,573,500.00
Surplus		2,403,548.90
Reserves		372,197.09
Total, corrected balance sheet beginning of year		$5,349,245.99
Additions: Capital stock sold		
3/31/18, par	$40,000.00	
Premium	20,000.00	
Total, effective 276 days	60,000.00	45,369.86
Total		$5,394,615.85
Reductions income tax, 1917	$659,110.79	
Additional income tax, 1916	6,328.91	
Total (deduct from above)		665,439.70
As shown on Schedule No. 2		$4,729,176.15

585 *Schedule 4—Explanation of items changed*

Pre-war income (commenced operating July, 1912):	
Net income 1913 (R. R. Company)	$21,398.41
Net income 1913 (Diamond)	176,310.93
Federal income tax paid 1913	844.62
Total	$198,553.96

bc—5

Pre-war invested capital:	
Capital stock January 1, 1913 (Diamond)	$1,147,400.00
" " " (R. R. Company)	83,500.00
Surplus " (Diamond)	60,043.69
" " (R. R. Company)	10,087.72
Total	$1,301,031.41

Schedule 5—Computation of excess-profits and war-profits credits

Consolidated net income taxable year (Schedule 1)	$3,765,355.05
Average consolidated net income pre-war period (Schedule 4)	198,553.96
Consolidated invested capital taxable year (Schedule 2)	$4,729,176.15
Average consolidated invested capital pre-war period (Schedule 4)	1,301,031.41
Increase in invested capital for taxable year as compared with average for pre-war period	$3,428,144.74

586	**Excess-profits credit:**	
	8% of invested capital for taxable year	$378,334.09
	Exemption	3,000.00
	Excess-profits credit	$381,334.09
	War-profits credit:	
	Average net income for pre-war period	$198,553.96
	Plus 10% of increase in invested capital as compared with average for pre-war period	342,814.47
	Total	$541,368.43
	Exemption	3,000.00
	War-profits credit	$544,368.43

Schedule 6—Computation of total tax (1918)

	Excess-profits tax:	Income	Tax
	Net income for taxable year	$3,785,355.05	
	Less excess-profits credit	381,334.09	
	Balance	$3,404,020.96	
	Taxable at 30%	564,501.14	$169,350.34
	" " 65%	2,839,519.82	1,845,687.86
			$2,015,038.22
	War-profits tax:		
	Net income for taxable year	$3,785,355.05	
	Less war-profits credit	544,368.43	
	Taxable at 80%	$3,240,986.62	$2,592,789.30
587	Less excess-profits tax		2,015,038.22
	War-profits tax		$577,751.08
	Total excess-profits and war-profits tax		$2,592,789.30
	Income tax:		
	Net income for taxable year	$3,785,355.05	
	Less:		
	Interest on obligations of United States not exempt $17,819.46		
	War-profits and excess-profits tax 2,592,789.30		
	Exemption 2,000.00	2,612,608.76	
	Taxable at 12%	$1,172,746.29	140,729.65
	Total war-profits, excess-profits, and income taxes		$2,733,518.85
	Previously assessed		1,074,749.11
	Additional tax to be assessed		$1,658,769.74

588–767 [Omitted.]

768 [Clerk's certificate to foregoing transcript omitted in printing.]

769–1019 [Omitted.]

1020 *Motion for judgment for plaintiff*

And now, January 23, 1929, comes counsel for plaintiff and moves the court that under the pleadings and all of the evidence in this case judgment must be entered for the plaintiff for the full amount of its claim.

JOHN W. DAVIS,
SMITH, SHAW, MCCLAY & SEIFERT,
Attorneys for Plaintiff.

Motion for judgment for defendant

Comes now the defendant, D. B. Heiner, by his attorneys, John D. Meyer, United States attorney for the western district of Pennsylvania, and John A. McCann, special assistant to the United States attorney, and moves the court for judgment in his favor and for his costs, on the ground that the pleadings and the evidence are insufficient to support a judgment in favor of the plaintiff.

JOHN D. MEYER,
United States Attorney for the Western District of Pennsylvania,
JOHN A. MCCANN,
Special Assistant to the U. S. Attorney,
Attorneys for the Defendant.

1021–1071 [Omitted.]

1072 In United States District Court

Opinion

GIBSON, District Judge.

This suit has been brought by the plaintiff against the defendant to recover alleged overpayments of 1918 and 1920 income taxes which were made over protest and pursuant to threats of distraint. A jury trial was waived by both parties.

From the testimony adduced before the court we make the following

FINDINGS OF FACT

1. Diamond Alkali Company, the plaintiff, is, and at all dates material herein was, a West Virginia corporation with its manfacturing plant at Painesville, Ohio, and its principal administrative office in the City of Pittsburgh, Pennsylvania.

2. D. B. Heiner, the defendant, is, and at the dates when the moneys herein sued for were paid was, the duly appointed, qualified and acting collector of internal revenue for the 23rd district of Pennsylvania. Said defendant resides in the borough of Kittanning and within the western district of Pennsylvania.

3. For 1918 and 1920 the plaintiff kept its books of account on the accrual basis and filed its Federal income and profits tax returns on the accrual and calendar year basis.

1073 4. The plaintiff filed its said returns for 1918 on June 16, 1919, and its said returns for 1920 on May 13, 1921.

5. Said return for 1918 showed an income and profits tax liability of $1,074,749.11, and said return for 1920 showed an income and profits tax liability of $263,891.89. Said sums were duly paid to the defendant and to his predecessor in office as collector of internal revenue for said 23rd district.

6. By letter dated July 11, 1927, the commissioner of internal revenue (hereinafter called the commissioner) notified the plaintiff that its said returns were erroneous, that the commissioner had made divers changes and adjustments in the plaintiff's tax liability and in the figures on which the same was computed, and that as the result of such changes and adjustments the plaintiff owed to the Government of the United States, in addition to said sums of $1,074,749.11 and $263,891.89 theretofore paid, income and profits taxes of $1,215,615.14 for 1918 and $60,769.03 for 1920, or the total sum of $1,276,384.17.

7. In and by said letter of July 11, 1927, the commissioner gave further notice to the plaintiff that the plaintiff had theretofore overpaid its income and excess profit taxes for 1919 by the sum of $1,467.64.

8. Pursuant to said letter of July 11, 1927, and on or about the 1st day of November, 1927, the commissioner, over the plain-

1074 tiff's protest, assessed against the plaintiff alleged additional income and profit taxes of $1,215,615.14 for 1918 and $60,769.03 for 1920. At or about the same time the commissioner issued certificate of overassessment for said overpayment of $1,467.64 for 1919.

9. Said sum of $1,467.64 overpaid by the plaintiff for 1919 was never refunded except by credit to 1918 tax. On or about November 7, 1927, this defendant applied said amount in part payment of said alleged additional tax of $1,215,615.14 for 1918.

10. On or about November 7, 1917, the defendant served upon the plaintiff written notice of said assessments of alleged additional taxes for 1918 and 1920 and demand for payment thereof, together with interest. Said notice gave credit of $1,467.64 on said alleged additional tax of $1,215,615.14 assessed for 1918, making the net claim of the defendant $1,214,147.50 for that year. The alleged additional tax for 1920 demanded by said notice was $60,769.03. On said net amount of $1,214,147.50 the defendant demanded interest of $117,739.08, and on said amount of $60,769.03, the defendant demanded interest of $5,892.93. Thus the total sum demanded by the defendant for alleged taxes and interest alleged to be owing thereon was $1,398,548.54.

11. Said demand of the defendant upon the plaintiff was accompanied with threats of penalties, further interest and seizures of the plaintiff's property if payment should not be made within ten days.

1075 12. Under duress and for the sole purpose of avoiding the penalties, further interest, and seizures threatened by the defendant as aforesaid, the plaintiff, under written protest, paid said total sum of $1,398,548.54 to this defendant on or about the 15th day of November, 1927.

13. The aforesaid sum of $1,215,615.14 with interest thereon of $117,739.08 was assessed and collected more than five years after plaintiff's return for 1918 was filed. The assessment and collection was made pursuant to authority claimed under certain waivers of the statute of limitations, hereinafter more particularly mentioned, entered into in writing by the Commissioner of Internal Revenue and the plaintiff. Of the aforesaid $1,215,615.14, principal sum, $1,027,227.75 resulted from the action of the commissioner as follows:

"(a) Final determination of the plaintiff's deduction for amortization of war-time facilities at $387,224.40, instead of permitting the same to stand at $1,344,465.15 as previously determined by the commissioner on or about December 1, 1921, whereby the plaintiff's deduction from 1918 gross income on account of amortization of war-time facilities was reduced from $1,245,448.21 to $315,956.89;

"(b) Disallowance of $439,104.16 of the total deduction, to wit, $876,366.71, taken by the plaintiff from gross income for 1918 on its books of account and on its returns to cover wear, tear, exhaustion, and obsolescence of its depreciable physical assets.

1076 "(c) Determination of 54.54+% under section 328 of the revenue act of 1918 as the ratio of plaintiff's excess profits tax to its net income instead of 45% as the plaintiff demanded."

14. The said alleged additional tax of $60,769.03 with interest thereon of $5,892.93 was assessed and collected more than five years after the plaintiff's return for 1920 was filed. Of the aforesaid $60,769.03, principal sum, $31,033.07 resulted from the action of the commissioner in reducing plaintiff's invested capital for 1920 by $574,372.90 on account of alleged additional income and profits taxes for 1917.

15. Of the alleged additional taxes for 1917 of $574,372.90, the defendant has confessed error as to $304,920.97, and the balance of $269,451.93 was assessed and collected subsequent to the expiration of the statutory period within which such collection might lawfully have been made and the liability of the plaintiff for said $269,451.93, if such liability ever existed, was extinguished.

16. Said alleged additional tax of $1,215,615.14 for 1918 was assessed and, together with interest thereon of $117,739.08, was collected by the defendant and paid by the plaintiff more than five years after the plaintiff's said return for 1918 was filed.

17. Said alleged additional tax of $60,769.03 for 1920 was assessed and, together with interest thereon of $5,892.93, was collected
1077 by the defendant and paid by the plaintiff more than five years after the plaintiff's said return for 1920 was filed.

18. Prior to the expiration of five years from the date that plaintiff's return for 1918 tax was filed, the Commissioner of Internal Revenue transmitted a certain unexecuted agreement wherein the plaintiff and the commissioner were the parties named, by the terms of which it was agreed that the time for the assessment and collection of said tax was extended beyond the statutory period fixed for assessment and collection. This agreement was signed by plaintiff and returned to the commissioner, who acknowledged the receipt thereof and stated that it was on file in his bureau. From time to time other such written agreements for extensions were transmitted by the commissioner to the plaintiff, signed by the plaintiff and transmitted to the commissioner and later acknowledged by the commissioner as received and filed in his office. By such written agreements the time for the collection of plaintiff's 1918 taxes was continued from time to time to December 31, 1927. None of said written agreements were signed by D. H. Blair, Commissioner of Internal Revenue, in person, but each of said agreements bear his signature, were on file in his office, and said commissioner placed reliance upon said written waivers in acting upon plaintiff's protests of assessments of plaintiff's 1918 taxes.

19. The plaintiff contructed, erected, installed, and acquired
1078 between April 6, 1917, and March 31, 1919, inclusive, certain buildings, machinery, equipment, and other facilities for the production of articles contributing to the prosecution of the war against the German Government. The cost of these facilities to the plaintiff, after depreciating to January 1, 1918, those installed during 1917, was $2,108,361.40.

20. A schedule of all of the aforesaid facilities, with the 1917 and 1918 costs, less depreciation, except a limestone dock costing $340,000, appears in the second column of Schedule I attached to defendant's Exhibit F, received in evidence at the trial. Said column is under heading "1917–1918 costs allowed less 1917 depreciation." Said second column of Schedule I of defendant's Exhibit F, excepting the item opposite the words "Raw material equipment," is incorporated in these findings by reference with like effect as if herein fully set forth. The item opposite the words "Raw material equipment" is stricken out, however, and replaced by the entry "$559,215.03," the original entry being increased by $340,000, the cost of the limestone dock aforementioned.

21. At the time of filing its said return for 1918 the plaintiff duly made claim for deduction from gross income under section 234 (a) (8) of the revenue act of 1918 on account of amortization of the said facilities, which claim was subsequently revised by the plaintiff and the revised claim for $1,756,453.64 filed with the commissioner on or about September 10, 1921.

1079 22. Sometime in September, 1921, the commissioner, acting by the authorized officials of the amortization section of the Income Tax Unit of the Bureau of Internal Revenue, sent his representative, one W. F. R. Griffith, an engineer in said amortization section, to the plaintiff's properties with written instructions and authority to examine the same, investigate the facts and matters set out in the plaintiff's said revised claim, audit said claim in the light of such investigation, and submit to said amortization section a report of the plaintiff's amortization allowance and a recommendation of said allowance and the amount thereof.

23. Said Griffith carried out his said instructions and on or about October 23, 1921, made a detailed written report to said amortization section covering his said examination and investigation and audit and his findings of fact in the course thereof and containing his conclusion and determination that the plaintiff was entitled to an amortization allowance of $1,344,465.15, of which $1,245,448.21 should be deducted from 1918 gross income and $99,016.94 from 1919 gross income.

24. In the ordinary and usual course of business of the Income Tax Unit and said amortization section thereof, said report and recommendation of Griffith came on for review before one B. L. Wheeler, Chief of Engineers in said amortization section and duly authorized by the commissioner in that behalf, and upon such review and
1080 consideration thereof the said B. L. Wheeler approved said report and recommendation in all respects, and on or about December 1, 1921, signified his approval in writing endorsed on said report.

25. On or about the 1st day of December, 1921, and in the ordinary and usual course of business of the Income Tax Unit and said amortization section, said report and recommendation came before one T. J. S. Kishpaugh, acting chief of said amortization section, who then and there approved said report and signified his approval by endorsement in writing thereon.

26. On or about the 2nd day of December, 1921, a copy of said report and recommendation, with said endorsements thereon, was delivered to the plaintiff by said amortization section on behalf of and with the authority of the commissioner, with an accompanying declaration to the effect that the amount of plaintiff's amortization deduction was tentatively, not finally, declared, and was subject to readjustment.

27. The commissioner did not at any time after December 1, 1921, and before March 3, 1924, make any reexamination or reinvestigation or further examination or investigation of the matter of the plaintiff's amortization allowance, or obtain any further facts or evidence with respect to the same, or take any further action whatsoever in that behalf, or determine that or consider whether said allowance of $1,344,465.15 was otherwise than correct.

1081 28. The plaintiff did not at any time subsequent to said determination of December 1, 1921, make any protest against

the amount or legality thereof or request any reexamination of its return in regard thereto, or request any examination or further examination or reexamination, or any investigation or reinvestigation or further investigation of the matter of its amortization allowance. On the contrary, the plaintiff accepted said determination as correct and proper and took no further action whatsoever with respect thereto.

29. Subsequent to March 3, 1924, to wit, on or about October 1, 1924, one L. E. Luce, an appraisal engineer in said amortization section, was assigned the matter of said allowance for reinvestigation and reexamination, but neither the said Luce nor any other person took any action in that behalf, nor was any further action taken in the Income Tax Unit with respect to the plaintiff's amortization allowance, until on or about April 1, 1925.

30. On or about April 1, 1925, the said Luce went to Painesville, Ohio, for the purpose of examining the plant of the plaintiff. He arrived at or about 10 o'clock a. m. and left at or about 4 o'clock p. m. on the same day.

31. On or about November 4, 1925, Luce made a report to the amortization section (then called appraisal section), stating in such report that $468,812.20 was the amortization deduction to which the plaintiff was entitled.

1082 32. The said last-mentioned report was entitled on the covering page thereof "Report on Redetermination of Amortization Claim of the Diamond Alkali Company, Pittsburgh, Pennsylvania." In the text of said document the report and determination of said W. F. R. Griffith was referred to as a "First determination" and the report of said Luce as a "First redetermination." Said report of Luce contained the further statement in the last paragraph thereof that it cancelled and superseded the said Griffith report and that "the allowances herein recommended are in lieu of those previously made." Said report of Luce was approved, by signed writing thereon, by Felder Furlow, reviewing engineer, and J. T. Keenan, then chief of said appraisal section (formerly amortization section).

33. On or about November 4, 1925, said appraisal section (formerly amortization section) sent to the plaintiff a copy of said so-called report on redetermination of amortization claim of the Diamond Alkali Company, Pittsburgh, Pennsylvania. The report was so sent at the plaintiff's request.

34. On or about November 17, 1926, the plaintiff received from said appraisal section (formerly amortization section) a paper entitled on the covering page thereof "Office Report on Second Redetermination of the Amortization Claim of the Diamond Alkali Company, Pittsburgh, Pennsylvania," wherein the plaintiff's amortization allowance was stated to be $387,224.40, of which

1083 $369,022.30 was apportioned to 1918 and $18,202.10 to 1919. Said so-called second redetermination was made by said L. E.

Luce in the first instance, without, however, any further examination of the plaintiff's properties, and was approved, by signed endorsement thereon, by M. W. Nolan, reviewing engineer in said appraisal section (formerly amortization section), and J. M. Clack, then chief of said section. In said "office report on second redetermination" said document of November 4, 1925, was referred to as "report on the first redetermination" and the said so-called office report on second redetermination contained in the last paragraph thereof a statement that "the allowances herein recommended are in lieu of those previously made."

35. Said so-called office report on second redetermination was used by the commissioner in his last computation of the plaintiff's net income for 1918 and in assessing the alleged additional tax for that year which is sought to be recovered in this action.

36. The allowances specified in said two reports of Luce were not based on the discovery of any fraud in connection with said first recommendation stated in said Griffith report, or on any new and material evidence not available to W. F. R. Griffith, or on any mathematical error or mistake in the said Griffith report.

37. At all times involved in this proceeding the plaintiff
1084 was engaged in the manufacture of alkali by the Solvay process. The basic product of plaintiff's plant was soda-ash or sodium carbonate. In 1913 and for several succeeding years soda-ash was the only product manufactured. Shortly before 1918 a department in the plant was established for the manufacture of caustic soda and in 1918 another department for the manufacture of baking soda. Subsequent to the amortization period still another department for the manufacture of washing soda was put in operation. Soda-ash is the base in caustic soda, bicarbonate of soda, and washing soda, and the facilities for the manufacture of these products were necessarily connected with, and involved in, the facilities for the manufacture of soda-ash. Numerous facilities were employed in each of the several steps required in the manufacturing processes of all of the products of the plaintiff company.

38. The said recommendation made on or about December 1, 1921, was predicated on the plaintiff's manufacturing plant being one harmonious unit or whole made up of mutually interdependent facilities as aforesaid, but said redeterminations or attempted redeterminations based on said reports of L. E. Luce were based on the theory that the plaintiff's plant, for amortization purposes, was composed of sections or parts severable from the unit or whole and not of mutually interdependent and non-severable facilities.

39. The capacity of the plaintiff's plant as a whole can be best stated or measured in terms of soda-ash, the chief and basic alkali product manufactured.

1085 40. The soda-ash capacity of the plaintiff's entire plant is fixed by the capacity of the furnaces employed in the final step of producing soda-ash.

41. At the end of the amortization period—that is, after the addition of war-time facilities and during the postwar period—there were forty-one soda-ash furnaces in plaintiff's plant. Under normal conditions not over four furnaces would be kept idle continuously for the purpose of making necessary repairs and adjustments; and not less than thirty-seven could be kept in continuous operation twenty-four hours per day three hundred and sixty-five days per year.

42. The capacity of each furnace at the end of the amortization period and during the postwar period was, under normal conditions, 33,250 tons of soda-ash per month.

43. The actual average per month production of the plaintiff's plant for the postwar period, to wit, March 3, 1921, to March 3, 1924, was 22,597 tons of soda-ash.

44. The plant of the plaintiff as enlarged by the war-time facilities, was in excess of the needs of the plaintiff during the postwar period.

45. The "value in use"—that is, the ratio of the actual use of the facilities to the use of which they were capable—during the
1086 postwar period is represented by the fraction 22597/33250, or 68%; and the percentage which represents the extent to which the facilities were not necessary for the postwar use is 32%.

46. A reasonable deduction on account of the amortization of plaintiff's war-time facilities acquired in 1917 and 1918 at a total cost (less depreciation of 1917 acquisitions) of $1,768,361.40 is $646,996.01. This amount should be spread over the year 1918 and the first three months of 1919 by allocating $553,957.98 to 1918 and $93,038.03 to 1919.

47. In determining the taxes of the plaintiff for 1917, 1918, 1919, and 1920, the commissioner found and used a rate of 10.4% per annum for wear, tear, exhaustion, and obsolescence (depreciation). This was a reasonable rate for that period.

48. In 1918, and throughout that year, laborers and operatives were untrained, of poor quality, and remained in employment brief periods of time. The plaintiff's labor turnover for that year was very great. Mechanics were, for the most part, new employees unfamiliar with the plaintiff's apparatus, relatively inexperienced as mechanics and too few in number. Under pressure from the Government and otherwise the plant was forced to such an extent that machinery was often continued in operation when it should have been shut down for repairs. Raw materials and fuel were of poor quality and poorly prepared and imposed an abnormal strain upon and damage to the plaintiff's apparatus.

1087 49. Plaintiff is not entitled to any sum for exhaustion, wear, tear, and obsolescence of its depreciable properties in addition to the amount allowed by the Commissioner of Internal Revenue, to wit, $437,262.55.

50. The plaintiff duly filed its income and profits tax returns for the calendar year 1917 on or about May 1, 1918, and paid to the then collector of internal revenue for the 23rd district of Pennsylvania

the taxes appearing by said returns to be owing. Subsequently, the commissioner asserted that the plaintiff owed additional income and profits taxes for 1917 in the sum of $574,372.90. In arriving at the alleged tax liability of the plaintiff for the year 1920, as set out in his letter of July 11, 1927, the commissioner deducted from plaintiff's invested capital for 1920 the aforesaid sum of $574,372.90, thereby reducing plaintiff's invested capital to $8,376,362.35. Of this reduction of plaintiff's invested capital the defendant has confessed error as to $304,920.97. The remainder of the reduction amounting to $269,451.93 was assessed and collected from the plaintiff over its written protest after the expiration of the statutory period within which collection might lawfully have been made.

51. On application by the plaintiff the commissioner found and so declared of record that the plaintiff's excess profits tax for 1918, if determined without the benefit of section 327 of the revenue act of 1918, would, owing to abnormal conditions affecting the capital
1088 or income of the plaintiff, work upon the plaintiff an exceptional hardship, evidenced by gross disproportion between the tax computed without the benefit of said section 327 and the tax computed by reference to the representative corporations specified in section 328 of the revenue act of 1918.

52. In computing the plaintiff's excess profits tax for 1918 under said section 328 the commissioner determined the ratio of tax to net income at 54.54%, arriving at that ratio, as he claimed, on the basis of the ratio of average tax to average net income (in excess of the specific exemption of $3,000) of representative corporations engaged in a like or similar trade or business to that of the plaintiff.

53. On or about the 23rd day of December, 1927, the plaintiff duly filed with the commissioner, on the forms prescribed by the commissioner for that purpose, claims for refund of the overpayments of taxes for 1918 and 1920 herein sought to be recovered.

54. Prior to the commencement of this action, to wit, on or about the 13th day of April, 1928, said refund claims and each of them were wholly rejected by the commissioner; and no part of what the plaintiff claims as overpayments of taxes and interest has been repaid or refunded.

55. Exhibit 1, attached hereto and made part hereof, is a computation of the taxes for 1918 and 1920, after deducting for amortization of war facilities in 1918 the sum of $143,029.05; and after increasing the invested capital for 1920 by the sum of $574,372.90.
1089 56. The plaintiff is entitled to judgment for the sum of $143,029.05, with interest thereon of $13,852.37, for overpayment of 1918 taxes, and $16,891.21, with interest thereon of $1,637.97, overpayment of 1920 taxes, the total being $175,410.60, with interest thereon from the date of overpayment, to wit, November 15, 1927.

EXHIBIT 1

Schedule, 1918 taxes

Net income		$3,821,143.63
Deduct additional amortization		238,001.09
		$3,583,142.54
Excess-profits tax, at 54.54%		1,954,245.94
Income tax:		
Net income		$3,583,142.54
Less:		
Profit tax	$1,954,245.94	
Liberty bond interest	17,819.46	
Exemption	2,000.00	
		$1,974,065.40
Balance taxable at 12%		$1,609,077.14
Excess-profits tax		$1,954,245.94
Balance at 12% tax		193,089.26
Total income and profits tax		$2,147,335.20
1090 Tax payments:		
With return		$1,074,749.11
November 15, 1927		1,215,615.14
Total payments		$2,290,364.25
Total due		2,147,335.20
Overpayment tax		$143,029.05
Interest overpaid		$13,852.37
(Interest at .09685 on $143,029.05.)		
1918 tax overpaid		$143,029.05
Interest overpaid		13,852.37
Total overpayment		$156,881.42

Calculation of tax based on court's decision for 1916, 1918, 1919, and 1920.

1920

Invested capital commissioner's letter—Exhibit 5		$7,346,041.07
Add:		
(a) Additional tax assessed by commissioner for 1917—admitted to have been deducted from invested capital in error		304,920.97
(b) Additional tax assessed by commissioner for 1917 in addition to (a) above, decided by the court to be refundable		269,451.93
1091 (c) Refund of tax allowed by court for 1916		6,325.77
(d) Refund of tax allowed by court for 1918		143,029.05
(e) Proration of refund of tax allowed by court for 1919—13,106.40×.4214		5,523.04
		$8,075,291.83
Deduct:		
Additional amortization allowed for 1918	$238,001.09	
Additional amortization allowed for 1919	49,525.73	
Total deduction		287,526.82
Corrected invested capital		$7,787,765.01
Net income		1,529,710.37
Excess-profits tax credit ($7,787,765.01×.08+$3,000)		624,021.29

Excess-profits tax:			
Net income		$1,529,710.37	
Less credit		624,021.20	
Taxable at 20%		$905,689.17	$181,137.83
Income tax:			
Net income		$1,529,710.37	
Less:			
Excess-profits tax	$181,137.83		
1092 Liberty bond int	80,253.71		
Exemption	2,000.00		
		263,391.54	
Taxable at 10%		1,266,318.83	126,631.88
Total tax			$307,769.71
Tax payments:			
With return		$263,891.89	
November 15, 1927		60,769.03	
Total tax			$324,660.92
			307,769.71
Overpayment taxes			$16,891.21
Interest overpaid			1,637.97
			$18,529.18
Interest paid Nov. 15, 1927		$5,892.93	
Or .096972 of $60,769.03.			
Interest at .096972 on $16,891.21		1,637.97	

CONCLUSIONS OF LAW

The claim of the plaintiff asserts improper assessment and collection from it of taxes for the years 1918 and 1920. First, it is alleged that the Commissioner of Internal Revenue assessed against the plaintiff, and the defendant wrongfully collected from it, a
1093 sum which should have been credited to plaintiff as a reasonable deduction from the latter's 1918 taxes for the amortization "of buildings, machinery, equipment, or other facilities, constructed, erected, installed, or acquired, on or after April 6, 1917, for the production of articles contributing to the prosecution of the present war." (Section 234 (a) (8) of the revenue act of 1918.) The second phase of the claim alleges an unlawful assessment and collection of an amount which properly should have been allowed plaintiff as a credit for depreciation upon its 1918 taxes. A third branch of the claim sets out a wrongful determination of plaintiff's excess-profits tax rate under special assessment (sections 327 and 328, revenue act of 1918) at 54.54% instead of 45%, as claimed by the plaintiff, and a following illegal collection by the defendant. A fourth phase of the claim asserts that the commissioner wrongfully assessed against plaintiff the sum of $574,372.90 as additional income and profits taxes for the year 1917, and, in the computation of plaintiff's taxes for 1920, improperly deducted such sum from the plaintiff's invested capital, thus making it appear that plaintiff's invested capital for 1920 was less in proportion to its income than was actually the case; and this wrongful deduction in the assessment

was followed by the defendant's illegal collection of the increase in tax thus improperly created.

We shall discuss each of these four contentions of plaintiff at greater length, but before doing so will notice another claim which relates to the entire amounts of 1918 and 1920 taxes for which suit has been brought. Such amounts were assessed on November
1094 1, 1927, and paid under protest on November 15, 1927, after rejection of refund claims. The plaintiff's returns for 1918 and 1920 were filed on June 16, 1919, and May 31, 1921, respectively, considerably more than five years before the assessment and collection of the amounts in question, and plaintiff has based upon this fact its contention that the collection was illegal because the statutory period therefor had expired.

Section 250 (d) of the revenue act of 1921 required a determination and assessment of the 1918 and 1920 taxes within five years after the return; and section 1106 (a) of the revenue act of 1926 provided that "the bar of the statute of limitations against the taxpayer in respect to any internal-revenue tax shall not only operate to bar the remedy but shall extinguish the liability." However, section 250 (d) of the act of 1921 and subsequent revenue acts have provided that the limitation shall not apply where the commissioner and the taxpayer have agreed in writing to a later determination, assessment and collection of the tax, and defendant justifies the collections in the instant action under this provision. As appears from the findings of fact, while plaintiff's petition for refund was pending, and prior to the expiraton of the collection period, the commissioner demanded the execution of a waiver by the plaintiff, which executed and returned the agreement required and in due time received an acknowledgment of its receipt by the commissioner and information from him to the effect that it was in force and on file in his office. Prior to the expiration of the waiver period,
1095 other like agreements extending the limitation period were executed by plaintiff and filed with the commissioner. The plaintiff denies the sufficiency of these waivers as a bar to the statute on the ground that they were not personally signed by the commissioner, nor even by one specifically authorized to do so. The testimoney does not disclose the actual signer of the waivers, but does make it plain that they were not signed by the commissioner in person. However, it would seem that the circumstances require the application of the presumption in favor of the regularity and validity of the acts of a public official. Personal signature of all such waivers on the part of the commissioner would be practically impossible and, we think, is unnecessary; and due authorization of another to sign for him is to be inferred from the commissioner's demands for the waivers, his acknowledgment of their receipt, the filing of them in his office, and his reliance upon them in passing upon plaintiff's application for refunds. The waivers offered in evidence by the defendant were sufficient, in our opinion, to toll the statute of limitations.

AMORTIZATION CLAIM

In this phase of plaintiff's claim, also, a question of limitation arises. One Griffith, an engineer in the amortization section of the Bureau of Internal Revenue, pursuant to a prior investigation, on October 23, 1921, filed a report wherein he recommended an allowance to plaintiff of $1,344,465.15 on account of amortization of its war facilities, of which amount, $1,245,448.21 was to be deducted from 1918 gross income, and $99,016.94 from 1919 gross income.

1096 On December 1, 1921, this report was approved by the chief of engineers of the amortization section and also by the acting chief of the section. On December 2, 1921, at plaintiff's request, a copy of Griffith's report was mailed to plaintiff. In the letter of transmittal plaintiff was informed that such report was not final and that no protest or request for modification would be considered until such time as the taxpayer should be notified of the result of the complete audit and examination. Subsequent to the transmittal of the letter of notification, a thirty-day period, taxpayer was informed, would be allowed for the presentation of objections to the allowance. Nothing was done in connection with plaintiff's amortization allowance prior to October 1, 1924, when one Luce, an engineer in the appraisal section (formerly the amortization section), was assigned to reexamine the matter. On April 1, 1925, Mr. Luce examined plaintiff's plant, and on November 4, 1925, filed a report where he recommended an amortization allowance to plaintiff of $468,812.30, of which amount $446,283.67 was to be deducted from 1918 income and $22,528.63 from 1919 income. On November 17, 1925, Mr. Luce filed a second report wherein he recommended an allowance for amortization of $387,224.40, of which amount $369,022.30 was to be deducted from 1918 income and $18,202.10 from 1919 income. The first report was entitled "Report on Redetermination of Amortization Claim," and the second, "Office Report on Second Redetermination." The second report was approved by the commissioner, who sent plaintiff the thirty-day letter, mentioned supra, wherein plaintiff was notified of the allowance approved.

1097 The plaintiff contends that the Griffith recommendation, when approved by the chief of engineers and the chief of the amortization section on December 1, 1921, was a determination of plaintiff's amortization deduction, and that the commissioner was prohibited from reexamining it at any time subsequent to March 3, 1924, by sections 234 (a) (8) of the revenue acts of 1918 and 1921. That section of the act of 1921, after providing for a "reasonable deduction" for amortization of war-time facilities, further provided:

"At any time before March 3, 1924, the commissioner may, and at the request of the taxpayer shall, reexamine the return, and if he then finds as a result of an appraisal or from other evidence that the deduction originally allowed was incorrect, the income, war profits,

and excess-profits taxes for the years affected shall be redetermined. * * *"

Just exactly what Congress had in mind, when the above-quoted part of section 234 (a) (8) was enacted, we do not undertake to surmise; but it plainly did not intend to prevent any examination of an amortization claim after March 3, 1924, on the part of the commissioner. To hold otherwise would be to ignore the proviso of section 250 (d) of the revenue act of 1921, which asserts:

"Provided further, That in cases coming within the scope of * * * or of paragraph (8) of subdivision (a) of section
1098 234 * * * the amount of tax or deficiency in tax due may be determined, assessed, and collected at any time; but prior to the assessment thereof the taxpayer shall be notified and given a period of not less than thirty days in which to file an appeal and be heard as hereinafter provided in this subdivision."

We are unable to accede to plaintiff's assertion that the approval of the Griffith report by the chief of engineers and the chief of the amortization section was a determination of plaintiff's amortization allowance. It is undoubtedly true that employes in the amortization section regarded and spoke of such approved reports as "determinations," despite the fact that they were still subject to audit, but the fact remains that the power of determination had not yet passed from the commissioner and did not pass from him prior to his issue of the thirty-day letter when the taxpayer was notified of his decision and given opportunity to appeal.

Plaintiff's amortization claim is not finally concluded by the failure of its contention in respect to the limitation of the commissioner's power to pass upon amortization deductions. It may, by the fair weight of the evidence, show that the commissioner's decision in respect to the proper amount of its amortization deduction was clearly wrong, and that it was compelled by the collector, the defendant, pursuant to that erroneous decision, to pay an amount not
1099 properly due the United States as a part of the amount of its 1918 taxes. If plaintiff so shows that it was entitled to an amortization allowance in excess of the amount determined by the commissioner, it is entitled in the instant action to a judgment for at least the amount of the excess.

The commissioner's determination of the amount of the amortization allowance was based entirely upon the recommendations of the second Luce report. Mr. Luce, in arriving at his conclusions, considered individual facilities, or facilities grouped by departments. He found that the plant originally had manufactured only soda ash; that a department had then been installed for the manufacture of caustic soda, and later departments had been added for the production of refined bicarbonate of soda. Soda ash is the base of caustic soda, bicarbonate of soda and washing soda. Mr. Luce also found that the plaintiff, during the war period beginning April 6, 1917, had also constructed various general plant facilities, such as a

machine shop, a locomotive shed, cooper shop, boilers, bridge crane, etc. After the war period the plaintiff added to its number of boilers, increased its caustic soda department, added a washing soda department, constructed an office building and a new boiler shop, a by-product coke plant and a cement plant. Plaintiff's records show that neither the caustic soda nor the refined bicarbonate departments had, during the postwar period, decreased its production of the war period, but on the contrary each was steadily increasing in output.

Luce therefore found that the postwar residual value of the
1109 war-time additions and establishment of these departments of the plant was equal to their war-time value, and therefore recommended no amortization allowance for them. The report alleged that the cooper shop was of minimum size for a plant such as that of the plaintiff, and denied amortization allowance thereon. In like manner he found full residual value in the machine shop and oil storage building, for each of which amortization was claimed. The same finding and recommendation was made in relation to certain miscellaneous equipment. The report also recommended disallowance of amortization deduction for a limestone dock and equipment, purchased at a cost of $340,000 during the war period. Certain special apparatus, including a flaking machine, six tank cars, an Oliver filter and an ash pit were granted the amortization deduction claimed by plaintiff. It was also recommended in the report that an allowance of 15% be made for amortization upon the boiler-house equipment, the amount awarded being $29,489.92 for 1918. Amortization was denied for real estate purchased for $205,969.10. The cost of the facilities for which amortization allowance was claimed for the years 1918 and 1919, less 1917 depreciation, was $3,099,988.83, and an allowance of $1,756,453.64 was claimed. From the total cost the approved report deducted the various costs which have been partially enumerated above, and which total $1,103,319.98 for the year 1918, and $141,572.43 for 1919. The total of costs for 1918, on which amortization is claimed, is $2,880,075.38. Excluding

the boiler-house equipment and tank cars, and other special
1101 equipment, mentioned above, of which the cost in 1918 was $39,889.46, also for which an amortization allowance of $18,833.76 was recommended, the report recommended an allowance of 21% upon the costs for 1917–1918 which had not been disallowed, less 1917 depreciation. The total allowance in amount was $369,022.30. In arriving at 21% of the war-time costs of the plaintiff as the proper amount for amortization allowance, Luce, in accordance with the general practice in the Bureau of Internal Revenue, multiplied the allowed costs of the facilities installed during the war period by a fraction, of which the numerator was the amount of plaintiff's average monthly production during 1923, the year of highest production, the postwar period (March 3, 1921, to March 3, 1924), and the denominator was the average monthly capacity of the plant at the end of the war. As representative of, and indicating the

capacity and production of the plant, soda ash, the basic product of the plant, was chosen as best representing the production and capacity of the plant. Mr. Luce, from the records of the plaintiff company, found that it had produced a monthly average of 26,163 tons of soda ash during the year 1923, and that the plant had a monthly capacity of 33,250 tons of the same product at the end of 1919. The fraction formed by monthly production over monthly capacity was approximately 79%, which was taken as the value in use of the facilities represented by the allowed costs, and the full cost value less the value in use, or 21%, was the portion of such allowed costs which represented the proper amortization allowance of plaintiff.

1102 The plaintiff asserts that Luce's calculation of its amortization allowance, adopted by the commissioner, was incorrect. While insisting that the Griffith report, approved as it was by his immediate superiors, and not having been overturned prior to March 3, 1924, was a final determination of its amortization deduction, it contends that if the matter were now open for consideration, an allowance of $1,245,448.21 would be correct. First, plaintiff attacks Mr. Luce's treatment of its plant as composed of several distinct departments, and his consequent exclusion from consideration for amortization allowance of costs incurred in the installation of facilities in certain of those departments which were alleged to have operated as fully during the postwar period as during the war. Its plant, says plaintiff, was one harmonious unit, and the extent of the use of the various facilities comprising the plant could not be determined separately or by departments, but only as a unit. It further says that the capacity and production of the plant can be accurately stated only in terms of soda-ash, the basic alkali product manufactured. Plaintiff concedes the propriety of arriving at an amortization allowance by a comparison of the postwar period production with the capacity of the plant at the end of the war, as was the practice in the Bureau of Internal Revenue, but insists that the Luce report not only unduly decreased the proper allowance by a disallowance of costs incurred in several departments, as hereinbefore set forth, but also erroneously increased the average monthly production of soda-ash and decreased the actual capacity of

1103 the plant, thus making it appear that the value in use of those facilities, for which costs had been allowed, was much greater than was actually the case. To put plaintiff's position in more concrete form, it is urged that plaintiff, upon its 1918 taxes, was entitled to an amortization allowance based upon an expenditure of $2,880,075.38 for war facilities during the years 1917 and 1918, such sum being the total amount then expended throughout the entire plant, without regard to the fact that part of it had purchased equipment for departments of the plant which manufactured more caustic soda and refined bicarbonate of soda in the postwar period than during the war period. In addition to its claim of error based on disallow-

ance of costs on the caustic soda and refined bicarbonate departments, plaintiff contends that the amount of soda ash manufactured during the postwar period was not an average of 26,163 tons per month but was 22,597 tons per month, and that the capacity of the plant to produce soda ash was not 33,250 tons per month but was 45,017 tons per month.

Considering the issue in respect to the disallowance of costs for facilities in the caustic soda and bicarbonate sections of the plant, we find no error in Mr. Luce's method in classifying the expenditures for such war facilities, and in excluding from the amortization equation such sums as went to purchase equipment which was in greater use in the postwar period than it had been in the war period. The statute prescribes no method for the determination of the proper amortization allowance. A general rule, such as adopted by
1104 the commissioner, is doubtless necessary as a matter of practice, but the commissioner might, if he saw fit, subject each separate facility to appraisal and specific determination of residual value rather than apply a general formula to part or all of the equipment of the plant under consideration for amortization. In our opinion, the action of the commissioner in approving the exclusion from the equation of the caustic soda and bicarbonate expenditures was justified by the testimony; which, with the exception later mentioned, also justifies the exclusion of the costs of the machine-shop building, the cooper shop, the oil-storage building and certain miscellaneous equipment, mentioned in Luce's schedule of costs upon which amortization was disallowed. All of such buildings and equipment were found to be no more than adequate for a plant having a production equal to that of the plaintiff during the postwar period.

The commissioner, by his approval of the Luce report, has excluded from the costs for which amortization was allowed an expense of $340,000 incurred in the purchase of a limestone dock and equipment. The exclusion was upon the ground that the dock was a necessity to the plant as a whole, and was only sufficient in size for the plaintiff's requirements. The testimony does not justify this exclusion, but fairly shows that the dock was approximately one-third larger than was required by plaintiff in the postwar period. We have therefore added this cost to those for which amortization has been allowed.

The commissioner, through Luce, to determine the residual
1105 value of plaintiff's 1917–18 facilities, used plaintiff's average monthly production of soda ash for 1923 as a numerator, and its production for that period determined in accordance with the multiplied by the number of furnaces under construction or completed, as a denominator, and multiplied the fraction so obtained, 26163/33250 (which equals 79%) by the allowed costs of the war-time facilities installed in 1917 and 1918. Plaintiff points to the fact that its production for 1923 was in excess of that of any other year of the postwar period, and contends that it was entitled to have its production for that period determined in accordance with the

ordinary usage of the Internal Revenue Bureau, by which the monthly average of the entire postwar period would be taken. It likewise attacks the finding of the examiner in respect to the capacity of its plant at the end of the war. It denies that the last ten months of 1918 fairly disclose the capacity, and points out the bad labor conditions of the period which, it asserts, prevented its furnaces from attaining full capacity. It attempts to fix that capacity by citing its production in June, 1924 (after the postwar period), when its furnaces averaged 40 tons of soda ash per day. It asserts that an average of 37 of its 41 furnaces can be kept in operation all the time, and that 40 tons fairly represents the daily soda-ash capacity of the plant.

The contention of the plaintiff in respect to the war-period production is justified, we think. In the interest of uniformity of practice and correct conclusion the monthly average output during the
1106 entire postwar period should be taken, rather than the average of the year of highest production. As to the capacity of the plant at the end of the war we have not been satisfied that the examiner was in error. The capacity claimed was attained only for a single month, and that after the close of the postwar period. The plant never exceeded the production of the last ten months of 1918 for any extended period. True, labor conditions were bad in those months and tended to reduce production, but on the other hand plaintiff was then straining to produce all the soda ash possible, and this effort undoubtedly offset the labor deficiencies to a large extent.

The testimony fairly establishes the postwar production of plaintiff as 22,597 tons of soda ash per month, and the capacity of the plant as 33,250 tons per month. Applying the commissioner's equation, the residual value of the plant was 68% and the plaintiff was entitled to an amortization allowance of 32% of the proper costs of its war-time facilities. The 1917 and 1918 costs for which amortization should properly be allowed amount to $2,108,361.40, after deduction of the 1917 depreciation. From this amount is to be deducted the costs of the boiler-house equipment, for which specific amortization allowance was fixed. The 1918 boiler-house equipment costs, less depreciation for 1917, amounted to $196,599.45, and the cost of the flaking machine, six tank cars, an Oliver filter and one ash pit, less depreciation, amounted to $39,889.46. Deducting these amounts from $2,108,361.40, we have $1,871,872.49 as the sum of the costs upon which plaintiff, in addition to the commissioner's specific
1107 amortization allowance, is entitled to receive an allowance of 32%, or $598,999.68, which, with the total of the special allowances, amounts to $646,996.01, the total amount of the amortization allowance to which plaintiff was entitled upon its 1918 return.

It is correct procedure to "spread" the deduction for amortization over the entire period the amortized facilities were in use as war-time facilities, and not credited only to the year in which the costs were incurred. The war-time period use, for the present purpose, was from January 1, 1918, to March 31, 1919. The income of plain-

tiff for 1918 was 85.62% of its total income for that period, and, therefore, that percentage of the amortization of 1918 costs has been allocated to 1918 income, and 14.38% of such costs to 1919 income. By this allocation the sum of $553,957.98 is deductible from 1918 gross income, and $93,038.03 from 1919 income. The commissioner having allowed an amortization deduction (allocated in the same proportions herein adopted) from 1918 income of $315,956.89, in arriving at plaintiff's correct tax for that year, a further deduction of $238,001.09 from the income of that year must be made. Such a deduction has been made in the schedule, attached hereto, showing a computation of plaintiff's 1918 tax.

DEPRECIATION

The commissioner allowed plaintiff a depreciation of $437,262.55 for 1918. This was based upon a 10.4% allowance, which in turn was founded upon an estimate that the average life of the
1108 facilities in plaintiff's plant was 9.6 years. The plaintiff does not attack 9.6 years as an unreasonable composite estimate of the probable useful existence of its plant for the years for which it was granted (1917–1920, each inclusive), but asserts that its machinery, largely by reason of its necessity to use inexperienced and inefficient laborers, wore out twice or three times as rapidly in 1918 as in other years. We are entirely satisfied that the labor situation did reduce the useful life of plaintiff's machinery more rapidly in 1918 than in other years, but that conclusion does not enable us to say that the commissioner's allowance for exhaustion, wear and tear and obsolescence for that year was inadequate; nor does it furnish any reason for an increase of the allowed amount which is based upon any proper theory. The plaintiff's contention, reduced to its essentials, is that the wear and tear upon its machinery was more than twice as great in 1918 as in 1917 or 1920, and that the commissioner, having allowed a composite rate of 10.4% for 1917 and 1920, should have fixed for 1918 a rate more than twice as large upon all of plaintiff's property upon which no amortization had been allowed. But tangible proof to establish the contention is lacking. Officers of the company have testified to the labor conditions and have expressed their estimate of its effect upon their plant; and they have also stated that much of their machinery was obsolescent. But there has been little, if any, testimony to specify the machinery replaced on account of wear and tear or obsolescence, or the cost of such machinery so replaced. On the other hand, there is evidence to
1109 the effect that much of the machinery subject to the hard usage of 1918 was still in use at the time of trial, and that the same was true in respect to the machinery alleged to be obsolescent in 1918. It also appeared that plaintiff had taken large credits against gross income for repairs upon machinery, and specific credits for particular machines abandoned. Such credits have the direct effect of reducing the allowance which plaintiff may rightfully demand for depreciation.

The plaintiff has the burden of proving that the commissioner's allowance was inadequate, and having failed to group its facilities, which vary in respect to length of existence, and to show the machinery replaced in use subsequent to 1918, and when replaced, or the amount expended for repair of such machinery which was charged against capital rather than gross income, we feel that it has failed to furnish such proof as would justify the court in finding that the commissioner was in error in his allowance.

DEDUCTION FROM INVESTED CAPITAL FOR 1920

The commissioner, in determining plaintiff's 1920 taxes, deducted from its invested capital $574,372.90. This amount was its alleged liability upon an additional assessment, since collected by defendant, for the year 1917. The commissioner has admitted that the reduction was incorrect as to $304,920.97, and has remitted the tax to that extent, but asserts, as does defendant, that $269,451.93 was properly deducted.

1110 The present action was tried at the same time as the case between the same parties at No. 5613. In that case the plaintiff seeks to recover $269,451.93, taxes for the year 1917 paid under protest, with $50,023.75, interest paid thereon, or a total of $319,475.68, with interest from the date of payment: also $6,325.77, with $1,166.66 interest, 1916 tax overpaid under the same circumstances. Upon consideration of the testimony in that case, we have determined that plaintiff is entitled to recover, as the payments were enforced after the expiration of the statutory period had both barred the remedy and extinguished the liability. This conclusion carries with it a finding that the deduction from invested capital for the year 1920 was incorrect, both as to the sum of $304,920.97, concerning which error has been confessed, and $269,451.93, which defendant maintains was properly deducted. The latter sum should, therefore, have been added to plaintiff's invested capital for 1920 in determining its tax for that year.

In addition to the case at No. 5613, another at No. 5761 was tried at the same time as the interest case. This case at No. 5761 was based upon an alleged overpayment of 1919 taxes. We found that plaintiff was entitled to a greater amortization deduction for 1919 costs than was given, and also that it should have had an additional amount to the sum allocated to it by the commissioner as an amortization allowance upon 1918 costs. The proper computation of plaintiff's tax for 1920 requires the addition to invested capital, as found by

1111 the commissioner, of $304,920.97, and $269,451.93, deducted in error by reason of illegal collection of 1916 and 1917 taxes, as aforesaid: also the addition of the refund of $143,029.05 on account of 1918 taxes, discussed supra in this opinion, and the commissioner's regulation proration of the refund of tax found to be overpaid for the year 1919 in the action at No. 5761. A computation of plaintiff's

1920 taxes is a part of the schedule attached to this opinion wherein the 1918 taxes are also computed. By it is shown an overpayment by plaintiff of $16,891.21 in settlement of its 1920 tax liability, and $1,637.97 interest thereon, or a total of $18,529.18. This sum is to be added to the sum of $156,881.42, tax and interest overpaid by plaintiff upon its 1918 taxes, as hereinbefore set forth.

EXCESS-PROFITS TAX RATE

The plaintiff, in addition to the amortization and depreciation claims in respect to the 1918 taxes, has sought a review of the commissioner's determination of its excess-profits tax rate for 1918. We feel that this court does not have jurisdiction to review the commissioner's ruling in this respect. See Williamsport Wire Rope Co. v. United States, 275 U. S. 520.

ORDER FOR JUDGMENT

And now, to wit, February 10, 1930, it is hereby ordered that judgment be entered for the plaintiff, Diamond Alkali Company, and against the defendant, D. B. Heiner, collector of internal
1112 revenue, in the amount of one hundred ninety-eight thousand nine hundred fifty-four and 59/100 ($198,954.59) dollars.

Per curiam.

G.

And now, to wit, April 19, 1930, exceptions noted to both plaintiff and defendant upon their respective requests for specific findings of fact which have not been incorporated in the findings of fact of the court, and bill sealed.

R. M. GIBSON, [SEAL.]
District Judge.

In United States District Court

Motion to vacate judgment

And now, to wit, this 14th day of February, 1930, comes Diamond Alkali Company, plaintiff above named, by its attorneys, Smith, Shaw, McClay & Seifert, and D. B. Heiner, collector, defendant above named, by John A. McCann, special assistant to United States attorney, and moves the court to vacate the judgment entered in the above-entitled case on February 10, 1930, for the following reasons:

Section 177 (b) of the Judicial Code as amended by section 615 of the revenue act of 1928, provides:

"(b) In any judgment of any court rendered (whether against the United States, a collector or deputy collector of internal reve-
1113 nue, a former collector or deputy collector, or the personal

representative in case of death) for any overpayment in respect of any internal-revenue tax, interest shall be allowed at the rate of 6 per centum per annum upon the amount of the overpayment, from the date of the payment or collection thereof to a date preceding the date of the refund check by not more than thirty days, such date to be determined by the Commissioner of Internal Revenue."

In the judgment entered herein, interest has been calculated on the principal sum to which the plaintiff is entitled under the opinion from the date of payment to the date of judgment.

The general counsel of the Bureau of Internal Revenue and the Comptroller General of the United States have requested that all such judgments be entered for the principal amount of tax and interest paid by plaintiff and which it is entitled to recover "with interest from the date of payment as provided by law." This facilitates the calculation of interest by the disbursing clerk of the Treasury Department.

Wherefore, both plaintiff and defendant pray this honorable court to vacate the aforesaid judgment and plaintiff prays that the court enter judgment providing for the payment of interest from the date of payment as provided by law; reserving to defendant, however, and to plaintiff, all rights to object and except to any judg-
1114 ment entered herein, on any other grounds than method of calculating interest under the revenue act of 1928.

SMITH, SHAW, MCCLAY & SEIFERT,
Attorneys for Plaintiff.
LOUIS E. GRAHAM,
United States Attorney.
JOHN A. MCCANN,
Special Assistant, United States Attorney,
Attorneys for Defendant.

Order

And now, to wit, February 14th, 1930, the foregoing motion having been presented in open court, upon consideration thereof and upon motion of the attorneys for the plaintiff, it is ordered that the judgment entered on February 10, 1930, herein, be vacated, and that judgment be entered for the plaintiff, Diamond Alkali Company, and against the defendant, D. B. Heiner, collector of Internal Revenue, in the amount of $175,410.60 with interest from November 15, 1927, as provided by law.

Exception reserved to plaintiff and bill sealed.

Exception reserved to defendant and bill sealed.

Per Curiam.

G.

1115 In United States District Court

Judgment

Thereupon, on the 14th day of February, 1930, pursuant to said order of the same date, judgment was entered as follows:

Feb. 14, 1930. Pursuant to the above order judgment is hereby entered for the plaintiff, Diamond Alkali Company, and against the defendant, D. B. Heiner, collector of Internal Revenue, in the amount of $175,410.60 with interest from Nov. 15, 1927.

J. Wood Clark, *Clerk.*

And now, to wit, April 23, 1930, the foregoing examined, approved, and agreed upon as the plaintiff's bill of exceptions herein, and further agreed that the order hereto annexed may be signed without further notice to either party.

Smith, Shaw, McClay, & Seifert,
Attorneys for Plaintiff.

Louis E. Graham,
United States Attorney.

John A. McCann,
Special Asst. to U. S. Atty.,
Attorneys for Defendant.

1116 In United States District Court

Order settling bill of exceptions

And now, to wit, April 23, 1930, in the furtherance of justice and that right may be done, and as certain matters and things above set forth do not appear of record in said cause, and to the end that said matters and things may be preserved in the record and presented to the honorable, the United States Circuit Court of Appeals for the Third Circuit, it is ordered, on motion of the attorneys for the plaintiff made in open court, that the foregoing be and hereby is allowed, settled, signed, sealed, and ordered filed as the plaintiff's bill of exceptions herein: this order being made and entered within the period in which an appeal may lie from the final judgment entered herein on the 14th day of February, 1930.

R. M. Gibson,
Judge of the District Court of
the United States for the Western
District of Pennsylvania.

[Clerk's certificate to foregoing transcript omitted in printing.]

1117 [Omitted.]

United States Circuit Court of Appeals for the Third Circuit

No. 4419 (List No. 48). October term, 1930

DIAMOND ALKALI CO., APPELLANT

vs.

D. B. HEINER, COLLECTOR, APPELLEE

On appeal from the District Court of the United States for the Western District of Pennsylvania

And now, to wit, this 15th day of January, A. D. 1931, it is ordered that Hon. J. Whitaker Thompson, district judge, for the Eastern District of Pennsylvania, and Hon. , district judge, for the District of , be, and he is hereby, assigned to sit in above case in order to make a full court.

JOSEPH BUFFINGTON, *Circuit Judge.*

[Endorsements:] 4419. Order assigning Hon. J. Whitaker Thompson for argument. Recd. & filed Jan. 15, 1932. Wm. P. Rowland, clerk.

United States Circuit Court of Appeals for the Third Circuit

No. 4426 (List No. 49). October term, 1930

D. B. HEINER, COLLECTOR, APPELLANT

vs.

DIAMOND ALKALI CO., APPELLEE

Appeal from the District Court of the United States for the Western District of Pennsylvania

And now, to wit, this 15th day of January, A. D. 1930, it is ordered that Hon. J. Whitaker Thompson, district judge, for the Eastern District of Pennsylvania, and Hon. , district judge, for the District of , be, and he is hereby, assigned to sit in above case in order to make a full court.

JOSEPH BUFFINGTON, *Circuit Judge.*

[Endorsements:]—4426. Order assigning Hon. J. Whitaker Thompson for argument. Recd. & filed Jan. 15, 1931. Wm. P. Rowland, clerk.

In the United States Circuit Court of Appeals for the Third Circuit

October term, 1930

No. 4419

DIAMOND ALKALI CO., APPELLANT

vs.

D. B. HEINER, COLLECTOR, APPELLEE

No. 4426

D. B. HEINER, COLLECTOR, APPELLANT

vs.

DIAMOND ALKALI CO., APPELLEE

And afterwards, to wit, 15th day of January, 1931, come the parties aforesaid by their counsel aforesaid, and this case being called for argument sur pleadings and briefs, before the honorable Joseph Buffington and honorable J. Warren Davis, circuit judges, and honorable J. Whitaker Thompson, district judge, and the court not being fully advised in the premises, takes further time for the consideration thereof.

And afterwards, to wit, on the tenth day of February, 1932, come the parties aforesaid by their counsel aforesaid, and the court, now being fully advised in the premises, renders the following decision:

In the United States Circuit Court of Appeals for the Third Circuit

No. 4419. October term, 1930

DIAMOND ALKALI COMPANY, APPELLANT

v.

D. B. HEINER, COLLECTOR, APPELLEE

No. 4426. October term, 1930

D. B. HEINER, COLLECTOR, APPELLANT

v.

DIAMOND ALKALI COMPANY, APPELLEE

No. 4427. October term, 1930

C. G. LEWELLYN, FORMERLY COLLECTOR, APPELLANT

v.

DIAMOND ALKALI COMPANY, APPELLEE

Upon appeals from the United States District Court for the Western District of Pennsylvania

Opinion

Filed February 10, 1932

Before BUFFINGTON, and DAVIS, Circuit Judges, and THOMPSON, District Judge

THOMPSON, Circuit Judge (sworn in as circuit judge February 3, 1931):

These cases were tried by the court below under a stipulation of the parties, without a jury. Diamond Alkali Company, the taxpayer, plaintiff below, was engaged in the manufacture of soda ash and related products. It filed its income and profits tax returns for the years 1918 and 1920 on June 16, 1919, and May 13, 1921, respectively, and paid the amounts shown therein as due. Thereafter the Commissioner of Internal Revenue assessed as additional taxes and interest the sum of $1,398,548.54 and collected the same on November 15, 1927, more than five years after the returns.

The plaintiff's claim for refund was rejected by the commissioner and suit was thereupon instituted in the District Court for the Western District of Pennsylvania as of No. 5762. Judgment was entered for the plaintiff in the sum of $175,410.60. The case is before this court on cross appeals Nos. 4419 and 4426.

Suit was also brought by the Diamond Alkali Company as of No. 5761 for the recovery of alleged overpayment of taxes for the year 1919. Judgment was entered for the plaintiff in that suit for $13,106.40. Appeals No. 4427 is taken by the collector of Internal revenue alone from that judgment.

Appeals Nos. 4419 and 4426

The plaintiff's claims for refunds for the years 1918 and 1920 were based on the following general contentions: That the Commissioner of Internal Revenue unlawfully assessed additional taxes for the years 1918 and 1920 after the statute of limitations had run; that the 1918 allowance for amortization of war-time facilities was inadequate; that the allowance for depreciation for 1918 and 1920 was inadequate; that the invested capital for 1920 was wrongfully

reduced by the unlawful collection of additional taxes for 1917; that the commissioner assessed excess-profits taxes for 1918 at a rate higher than that lawfully applicable.

The District Court held that the additional assessment for 1918 and 1920 was not barred by the statute; that the amount allowed for amortization by the commissioner was inadequate in several respects; that the amount allowed for depreciation was lawfully ascertained; that the plaintiff was entitled to have its 1920 invested capital increased by sums collected as additional taxes and interest for 1917; and that the court had no power to revise the rate fixed by the commissioner under the special assessment provisions. In addition, it directed that the amount allowed for amortization be allocated to the years 1918 and 1919.

Statute of limitations

The plaintiff contended that it was entitled to a refund of all additional taxes assessed and collected after the statute of limitations had run, and based its contention upon section 250 (d) (1) of the revenue act of 1921, which reads as follows:

"The amount of income, excess-profits, or war-profits taxes due under any return made under this act for the taxable year 1921 or succeeding taxable years shall be determined and assessed by the commissioner within four years after the return was filed, and the amount of any taxes due under any return made under this act for prior taxable years or under prior income, excess-profits, or war-profits tax acts, or under section 38 of the act entitled 'An act to provide revenue, equalize duties, and encourage the industries of the United States, and for other purposes,' approved August 5, 1909, shall be determined and assessed within five years after the return was filed, unless both the commissioner and the taxpayer consent in writing to a later determination, assessment, and collection of the tax; and no suit or proceeding for the collection of any such taxes due under this act or under prior income, excess-profits, or war-profits tax acts, or of any taxes due under section 38 of such act of August 5, 1909, shall be begun, after the expiration of five years after the date when such return was filed, but this shall not affect suits or proceedings begun at the time of the passage of this act: * * *."

Prior to the expiration of the five-year period, the commissioner transmitted to the plaintiff an unexecuted agreement, by the terms of which the time for the assessment and collection of the 1918 taxes was extended beyond the statutory period. The agreement was signed by the plaintiff and returned to the commissioner, who acknowledged its receipt and stated that it was on file in his office. From time to time similar written agreements were transmitted by the commissioner to the plaintiff, signed by the plaintiff, and returned to the commissioner, extending the time for assessment and collection to December 31, 1927. Although no one of the agreements was signed by the Commissioner of Internal Revenue in person, all

of them were signed in his name, were on file in his office, and were relied upon by him in acting upon the plaintiff's protests. The letters to the plaintiff with reference to the extension agreements went out in the regular course of business and were signed in the name of the assistant to the commissioner.

The cited statute requires only that the commissioner and the taxpayer consent in writing to the later determination, assessment and collection. It does not require that the consent, in order to be valid, be in one instrument or in any particular form. In the instant case, the consent by the commissioners is found in the letters which were sent out from his office. Contentions against the validity of agreements of extension, because of the lack of the commissioner's signature, were unsuccessfully made in this court in Liberty Baking Company v. Heiner (37 F. (2d) 703). (See also Trustees for Ohio and Big Sandy Coal Company v. Commissioner, 43 F. (2d) 782 (C. C. A. 4); Sabin v. United States, 44 F. (2d) 70 (Ct. Cls.); Stern Bros. & Co. v. Burnet, 51 F. (2d) 1042 (C. C. A. 8).) In Stange v. United States (282 U. S. 270, 276) the court said:

"As pointed out in Florsheim Bros., etc., v. United States (280 U. S. 453, 466), a waiver is not a contract, and the provision requiring the commissioner's signature was inserted for purely administrative purposes and not to convert into a contract what is essentially a voluntary, unilateral waiver of a defense by the taxpayer."

We find no error in the conclusion of the District Court that the additional assessments for 1918 and 1920 were made within the proper statutory period as extended by the waivers.

Amortization

One of the contentions upon which the plaintiff relies in support of its claim for refund is based upon the commissioner's treatment of its claims under section 234 (a) (8) of the revenue act of 1918. In order to reimburse those who had incurred capital expenditures in their business for war purposes, that act provides:

"In the case of buildings, machinery, equipment, or other facilities, constructed, erected, installed, or acquired, on or after April 6, 1917, for the production of articles contributing to the prosecution of the present war, * * * there shall be allowed a reasonable deduction for the amortization of such part of the cost of such facilities * * * as has been borne by the taxpayer, but not again including any amount otherwise allowed under this title or previous acts of Congress as a deduction in computing net income. * * *"

The plaintiff constructed, erected, installed, and acquired after April 6, 1917, certain buildings, machinery, equipment, and other facilities for the production of articles contributing to the prosecution of the war against the German Government. With its income-tax return for 1918 it filed a claim for a deduction from gross income on account of the amortization of the cost of such facilities.

One Griffith, an engineer of the amortization section of the Bureau of Internal Revenue, made an investigation of the facts set out in plaintiff's amortization claim and about October 23, 1921, submitted a report in which he recommended an amortization allowance in the amount of $1,344,465.15. The report was approved by the chief of the amortization section. On December 2, 1921, in response to a request by the plaintiff, a copy of the report was sent to it accompanied by a letter which read as follows:

"Further reference is made to your letter of November 7, 1921, and reply from this office under date of November 9, 1921, making request for copy of report by the appraisal engineer who made investigation of the facilities involved in claim for amortization.

"Copy of the approved report submitted by the appraisal engineer is enclosed for your information.

"In transmitting a copy of this report, at the present time, upon request of the taxpayer, it is to be clearly understood that the merits of the case, and the correctness of the conclusions reached by the engineer, are not now to be made the subject of objection or conference, and that no further consideration can be given to the amortization claim until such time as the taxpayer is officially notified of the result of the complete audit and examination. Subsequent to transmittal of the usual formal letter, there is provided a thirty day period wherein any objections by the taxpayer may be properly presented for the consideration of this office. The amortization feature of the case may be taken up only at that time, together with any other matters which the taxpayer may then desire to present."

Subsequent to March 3, 1924, the matter was assigned for reinvestigation to one Luce, another appraisal engineer in the amortization section. His final recommendation, made November 17, 1926, modifying a prior report of November 4, 1925, was that the plaintiff be allowed an amortization deduction of $387,224.40. The Commissioner of Internal Revenue based his determination of the amortization allowance on the Luce report.

It is contended by the plaintiff that the amortization allowance had been determined following the Griffith report and that any redetermination after March 2, 1924, was in violation of section 234 (a) (8) of the revenue act of 1921, which reads:

"* * * At any time before March 3, 1924, the commissioner may, and at the request of the taxpayer shall, reexamine the return, and if he then finds as a result of an appraisal or from other evidence that the deduction originally allowed was incorrect, the income, war-profits, and excess-profits taxes for the year or years affected shall be redetermined; * * *."

But that contention leaves out of consideration the effect of section 278 (b) of the revenue act of 1924, which reads:

"Any deficiency attributable to a change in a deduction tentatively allowed under * * * paragraph (8) of subdivision (a) of section 234 of the revenue act of 1918 or the revenue act of 1921

may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time."

We find no error in the finding and conclusion of the trial judge that the letter of December 2, 1921, fixed the deduction, reported by Griffith prior to March 3, 1924, as tentative and not final; nor in his conclusion of law that the power of determination had not yet passed from the commissioner, and did not pass from him prior to his issue of the thirty-day letter.

The final allowance followed the Luce report in November, 1926. Section 234 (a) (8) of the act of 1921 applies only in those cases in which the commissioner, having once determined and finally and not tentatively allowed the amortization deduction, then redetermines it. Under such circumstances the dead line is March 3, 1924. Under authority of section 278 (b), above cited, the commissioner had power to determine the deduction tentatively allowed at any time, and to collect in accordance with such determination.

In the cases of Commissioner v. Ohio Falls D. & F. Works, 50 F. (2d) 660, and Norton Co. v. Commissioner, 50 F. (2d) 664, the Sixth and First Circuits decided on the facts before them that the right granted to the commissioner by section 278 (b) to assess or collect deficiencies at any time was unavailable, since in each of those cases there had actually been more than a "tentative" allowance of the amortization deduction prior to March 3, 1924. In the instant case, the correspondence in the record and the finding of the trial judge convince us that any so-called allowance made immediately following the Griffith report and prior to March 3, 1924, was "tentative" within the meaning of section 278 (b).

In the court below, as previously indicated, the plaintiff contended that the method of computing the amortization allowance followed by the commissioner was erroneous; and that the commissioner improperly rejected claims for amortization upon the cost of a limestone dock and upon the cost of real estate purchased by the plaintiff during the war. Those subjects are discussed in the order named.

The plaintiff's plant had been enlarged by war-time facilities which were in excess of the needs of the plant during the post-war period, and it was therefore entitled to a deduction for amortization. The post-war period comprises the period between March 3, 1921, the date of the President's proclamation, and March 3, 1924. (U. S. Comp. Stat., sec. 3115 14/15 f.) During that time the plaintiff's plant produced an average of 22,597 tons of soda ash per month, and for the year showing peak production an average of 26,163 tons per month.

In order to ascertain the amount of the amortization allowance, the commissioner proceeded to determine the "value in use" or the "residual value," as it is commonly termed, of the war-time facilities. For that purpose he used the ratio which the post-war production bore to the war-time capacity, taking as the numerator of the fraction, representing the ratio, the post-war production and as the denominator of the fraction the war-time plant capacity. The

plaintiff had presented its claim to the Commissioner on the broad principles of this formula. The figures which it used were:

22,597 tons per month (average post-war production per month).
45,017 " " " (war-time capacity).

The commissioner substituted the following figures:

26,163 tons per month (average per month of the post-war year showing peak production).
33,250 " " " (war-time capacity).

The District Court found from the evidence, as a fact, that the average war-time capacity of the plaintiff's plant was 33,250 tons per month and not 45,017 tons, as claimed by the plaintiff. The commissioner and the court took the average war-time monthly production of 33,250 tons as plant capacity. That method might be justified if supported by the evidence. The witnesses, however, including the plaintiff's president, two industrial superintendents, and the former chief of the amortization section of the Bureau of Internal Revenue, unequivocally testified that the average monthly capacity of the plaintiff's plant was 45,017 and gave their reasons and the facts upon which they based their conclusion. The only testimony to the contrary was that of Luce. His testimony was based entirely on production records under war-time conditions. This was not a fair criterion by which to determine plant capacity. The court might have disbelieved the plaintiff's witnesses, but he did not base his conclusions upon that ground. It is apparent that he ignored the testimony of skilled and experienced witnesses, based upon actual facts, and reached a conclusion contrary to their testimony, without any substantial evidence to sustain his conclusion. The question before him was not the average plant production during the war, but the plant capacity. The learned judge must be held in error in his adoption of the figure of 33,250 tons as plant capacity, instead of 45,017 tons.

The trial judge, in finding the numerator of the fraction representing the ratio which post-war production bore to war-time capacity, rejected the commissioner's selection of the post-war year showing the peak production and adopted the contention of the plaintiff that the numerator should represent the average production of the plant per month during the whole post-war period, and therefore found the value in use to be $\frac{22,597}{33,250}$ or 67+%.

Section 234 (a) (8) of the revenue act of 1918 provides that there shall be allowed "a reasonable deduction" for amortization. The regulations and the practice adopted by the commissioner provide for arriving at a deduction through means of a ratio showing the relation of war-time capacity to post-war production. To be "reasonable," the allowance must be, as the term implies, just, fair, and equitable. The regulations of the commissioner provide for using a ratio as a means of comparison and that method would be just, fair, and equitable, if properly applied. But the term "ratio" in itself means the relation which one quantity has to another of the same

kind. In attempting to fix a ratio, the commissioner adopted a standard by which one terms of the ratio (the numerator) is represented by the average production during one year only of the post-war period, that of peak production, and the other term (the denominator) by the monthly average production of the whole war-time period. The defendant contended vigorously for the figures representing the average monthly production during the war-time period and prevailed in having his theory adopted and in obtaining a finding by the trial judge of the figures representing that standard. In attempting to arrive at the term of the ratio representing the post-war period, however, he urged the adoption of the average production during the peak year of that period and not during the whole period. We can not agree that a just and fair relation between the two periods can be obtained by the inconsistent method proposed to be applied by the commissioner and urged on his behalf by the defendant. In our view, in order to obtain a reasonable allowance which is just, fair, and equitable, the quotient should be that of the ratio of similar terms.

The commissioner considered specific facilities or groups of facilities in computing the allowance. The plaintiff claimed that its plant was one harmonious unit and that the extent of the use of the various facilities comprising the plant could not be determined separately or by departments but only as a unit. All the pertinent facts were before the learned district judge in his capacity as a fact-finding tribunal. Under R. S. sec. 649 (28 U. S. C. A., sec. 773) the findings of fact by a judge, in the event that a jury has been waived, have the same effect as the verdict of a jury. The findings will not be disturbed where there is any evidence to sustain them. (Tarn v. United States, 16 F. (2d) 272 (C. C. A. 3); Ward v. Joslin, 186 U. S. 142.) In the latter case it was said:

"When a case is tried by the court without a jury, its findings on questions of fact are conclusive, although open to the contention that there was no evidence on which they could be based."

It nowhere appears that it was impossible to fix a value on the individual facilities and no sound reason is advanced by the plaintiff to induce the court to reverse the commissioner's action. No facts appear to support the plaintiff's contention that the absolute unity of the plant for amortization purposes is established. Section 234 (a) (8) of the revenue act of 1918 bases amortization upon "facilities" and not upon the aggregate of the facilities united in one plant. In United States v. Briggs Mfg. Co. (40 F. (2d) 425, (C. C. A. 2)) specific facilities were considered by the commissioner in determining the amortization allowance. In appeal of Manville Jenckes Co. (4 B. T. A. 765) it is said:

"The deduction contemplated by the statute is 'a reasonable deduction for the amortization of such part of the cost of such (amortizable) facilities or vessels as has been borne by the taxpayer.' The deduction is in respect of specific facilities."

We find no error in the classification of facilities by the District Court.

The plaintiff purchased a limestone dock in 1917 at a cost of $340,000. The District Court permitted 32 per cent amortization on the total cost of the dock. The commissioner had disallowed any amortization. The defendant contends that the dock was purchased from an affiliated company, the Fairport, Painesville & Eastern R. R. Company, and that amortization does not apply to property transferred from one affiliated company to another. The record does not contain any proof convincing to the trial court that the plaintiff corporation was affiliated with that company in 1917, the year in which the dock was purchased. There is sufficient testimony to warrant the trial court's finding of fact that the limestone dock was in excess of the plaintiff's peace-time requirements. We therefore find no error in the allowance of 32 per cent on the cost of the dock. In view of our approval of the allowance by the District Court of amortization on the cost of the dock, it is directed that the depreciation allowed by the commissioner on the same cost be deducted from the determined amortized allowance.

The plaintiff claimed full amortization on the cost of land purchased by it at the total cost of $96,989.60 in 1917 and $108,979.50 in 1918. The purchase was made in order to settle actions for damages brought against the plaintiff by the owners of the land. It was conceded that no part of the plaintiff's plant was erected upon the land and that it was wholly useless to the plaintiff both during and after the war. The comissioner refused to make any allowance on the ground that land is not subject to amortization. The statute permits an amortization allowance on "buildings, machinery, equipment, or other facilities." Amortization is therefore limited to the facilities named or those *ejusdem generis*. (United States v. Baumgartner, 259 Fed. 722.) Finally the land was not used for the production contemplated by Congress. The case of United States v. Corono Coal Co. (23 F. (2d) 673), cited by the plaintiff, is readily distinguished from the case at bar. In that case amortization was allowed on the cost of a shaft driven through earth and rock to get at coal. A mining shaft is obviously a facility necessary to mining operations. The land for which amortization was claimed does not come within the class meant by Congress by the phrase "other facilities."

The District Court allocated the allowance for amortization over the years 1918 and 1919 in accordance with the percentages previously determined by the commissioner. Article 185 of Regulations 62 of the Treasury Department provides that an amortization allowance shall be apportioned in cases where the property was employed in the production of articles contributing to the prosecution of the war over the respective accounting periods of the taxpayer, having reasonable regard to the gross income and net income. The defendant contends that, since the court altered the income from that established

by the commissioner, through an additional amortization allowance, it should alter the percentage of such an allowance deductible in each year. The regulations, however, provide that:

"The amortization allowance shall be spread in proportion to the net income (computed without benefit of the amortization allowance) * * *."

It is therefore obvious that the percentages for the years 1918 and 1919, as determined by the commissioner, are unaffected by the increased amortization allowance.

Depreciation

The commissioner allowed a composite depreciation rate of 10.4 per cent for all of the plaintiff's depreciable assets for the years 1917 and 1920, inclusive. This amounted to $437,262.55 for 1918, less than half the $876,366.71 claimed by the plaintiff. The District Court sustained the action of the commissioner.

The plaintiff does not complain of the depreciation rate which was applied for 1917, 1919, and 1920, but insists that the rate for the year 1918 should be 20 per cent or more. The basis for this contention is that, during that year, poor labor conditions resulting in direct damage to and neglect of the machinery, inadequate repairs due to the lack of mechanics, and poor fuel caused a rapid deterioration of the plant. Whether the amount the commissioner caused to be deducted for depreciation under those circumstances was right is a question of fact. The burden of proving the contrary is on the taxpayer. We said in Rieck v. Heiner (25 F. (2d) 453; certiorari denied, 277 U. S. 608):

"Nor is there a burden on the commissioner, when he has formerly determined an amount of depreciation, to prove it right as a condition to sustaining the assessment by showing the investigation he has pursued and the matters that have influenced his judgment in arriving at it, for having found the depreciation and having made an assessment based on it, the law presumes his action right and the assessment prima facie valid."

The plaintiff did assume the burden of proving that the depreciation rate allowed by the commissioner for 1918 was wrong, but, in the judgment of the trial judge, failed. We see no error in his conclusion.

The revenue acts of 1918 and 1921, sections 234 (a) (7), provide that, in computing the net income of a corporation subject to tax, "a reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance allowance for obsolescence" shall be made. While a "reasonable" allowance is not defined in the statutes, we have hereinabove defined it as one that is just, fair, and equitable.

Although the deduction allowable on account of depreciation is to be based upon the actual wear and tear sustained during that

year, it is obvious that actual wear and tear of machinery and equipment is not ordinarily susceptible of scientific measurement in any one year. The commissioner determined that the average life of the equipment in the plaintiff's plant was from nine to ten years, and therefore determined the composite depreciation allowance of 10.4 per cent. The plaintiff can not take credit for an accelerated depreciation rate for the one year of 1918 without subjecting its taxes for 1917, 1919, and 1920 to revision by the commissioner. The commissioner's determination of the rate of depreciation will not be disturbed in the absence of fact findings sufficient to convince us of error in law by the court below.

The plaintiff contends that it was entitled to a deduction for depreciation at the proper rate upon the unamortized cost of its war facilities. The defendant maintains that, in computing the residual value of the property, the depreciation factor had already been considered. The District Court did not pass upon this contention in its findings of fact or conclusions of law. In the absence of any reference in the briefs of either party to facts upon the record sustaining their respective contentions, we do not deem this question properly presented for decision.

Invested capital for 1920

The District Court filed its opinion February 10, 1930. At that time there was a judgment in favor of the plaintiff for an alleged overpayment of taxes for 1916 and 1917 in the case of Diamond Alkali Company v. Heiner (39 F. (2d) 643). The basis for that judgment was that these taxes had been collected after the expiration of the appropriate statutory limitation period. Subsequent to the filing of the opinion of the District Court in the case at bar, an appeal, taken by the defendant to this court from the judgment rendered in that case, was decided in favor of the defendant. (See Heiner v. Diamond Alkali Company, 49 F. (2d) 120.) That decision is sustained by that of the Supreme Court in Graham and Foster v. Goodcell (282 U. S. 409). Since the judgment in favor of the plaintiff for the alleged overpayment of taxes for 1916 and 1917 has been reversed by this court, the plaintiff is not entitled to have the sum of $269,451.93 credited to its 1920 capital, as directed by the court below. The District Court was therefore in error in holding that the capital of the plaintiff for 1920 should be thus increased.

Special assessment

Upon application of the plaintiff, the commissioner found that its excess-profits tax for 1918, as determined without the benefit of section 327 of the revenue act of 1918, would, owing to abnormal conditions affecting its capital or income, work upon it an exceptional hardship evidenced by gross disproportion between the tax computed

without the benefit of the said section and the tax computed by reference to the representative corporations specified in section 328. The commissioner determined the amount due as plaintiff's excess-profits tax for 1918 as $2,084,324.26 on the basis of a net income of $3,821,143.63. The ratio of tax to net income therefore, as determined by the commissioner, was 54.54 per cent. The plaintiff's contention in the District Court was that the rate of 54.54 per cent was not justified by the evidence and that the rate should be 45 per cent. The District Court having reduced the net income for 1918 and applied the rate determined by the commissioner, to wit, 54.54 per cent, to the reduced income, the contention was abandoned. The defendant's position, on appeal, is that, the District Court being without jurisdiction to review the action of the commissioner in determining whether a special assessment should be made under sections 327 and 328 of the revenue act of 1918 (Williamsport Wire Rope Company v. United States, 277 U. S. 551; see also Cramer & King Co. v. Commissioner, 41 F. (2d) 24), it follows that the commissioner's action in determining the amount of the plaintiff's excess-profits tax under sections 327 and 328 is not subject to judicial review.

In Brown's "Shamrock" Linens, Ltd., v. Bowers (41 F. (2d) 862) the commissioner had allowed a special assessment and computed the excess-profits tax in accordance with section 328 of the revenue act of 1918 at the rate of 44.8 per cent of its net income. The taxpayer complained that the rate was excessive and should have been 25 per cent. The court there held that section 328 vested in the commissioner administrative discretion in the computation of the tax and that his discretion was not subject to judicial review. This ruling was affirmed by the Circuit Court for the Second Circuit in 48 F. (2d) 103. The question appears to have been settled by the Supreme Court in favor of the commissioner's contention when it refused a certiorari in Brown's "Shamrock" Linens, Ltd., v. Bowers, Executor (283 U. S. 865).

The District Court was therefore in error in redetermining the amount of the excess profits tax fixed by the commissioner.

Appeal No. 4427

We have disposed of the questions involved in this appeal in the opinion upon Appeals Nos. 4419 and 4426.

The cases will be remanded to the District Court for modification of its judgments in accordance with the foregoing opinion.

A true copy. Teste:

_____,

Clerk of the United States Circuit Court of Appeals for the Third Circuit.

In the United States Circuit Court of Appeals for the Third Circuit

No. 4419 (List No. 48). October term, 1930

DIAMOND ALKALI COMPANY, APPELLANT

vs.

D. B. HEINER, COLLECTOR, APPELLEE

On appeal from the District Court of the United States for the Western District of Pennsylvania

This cause came on to be heard on the transcript of record from the District Court of the United States, for the Western District of Pennsylvania, and was argued by counsel.

On consideration whereof it is now here ordered and adjudged by this court that the judgment of the said District Court in this cause be, and the same is hereby, modified, with direction to the said District Court to enter a new judgment in accordance with the opinion of this court.

Philadelphia, February 10, 1932.

J. WHITAKER THOMPSON,
Circuit Judge.

[Endorsements:] 4419. Order modifying judgment, etc. Recd. & filed Feb. 10, 1932. Wm. P. Rowland, clerk.

In the United States Circuit Court of Appeals for the Third Circuit

No. 4426 (List No. 49). October term, 1930

D. B. HEINER, COLLECTOR, APPELLANT

vs.

DIAMOND ALKALI CO., APPELLEE

On appeal from the District Court of the United States for the Western District of Pennsylvania

This cause came on to be heard on the transcript of record from the District Court of the United States for the Western District of Pennsylvania, and was argued by counsel.

On consideration whereof it is now here ordered and adjudged by this court that the judgment of the said District Court in this cause be, and the same is hereby, modified, with direction to the said District Court to enter a new judgment in accordance with the opinion of this court.

Philadelphia, February 10, 1932.

J. WHITAKER THOMPSON,
Circuit Judge.

[Endorsements:] 4426. Order modifying judgment, etc. Recd. & filed Feb. 10, 1932. Wm. P. Rowland, clerk.

United States Circuit Court of Appeals for the Third Circuit

October term, 1930

No. 4419

DIAMOND ALKALI COMPANY, APPELLANT

against

D. B. HEINER, COLLECTOR, APPELLEE

No. 4426

D. B. HEINER, COLLECTOR, APPELLANT

against

DIAMOND ALKALI COMPANY, APPELLEE

No. 4427

C. G. LEWELLYN, FORMERLY COLLECTOR, APPELLANT

against

DIAMOND ALKALI COMPANY, APPELLEE

Upon appeals from the United States District Court for the Western District of Pennsylvania

John W. Davis, William A. Seifert, Maynard Teall, Marion N. Fisher, counsel for the Appellant, Diamond Alkali Company.

[Endorsed:] Recd. & filed Mar. 5, 1932. William P. Rowland, clerk.

Petition of appellant for rehearing

To the Honorable the Justices of the Said Court:

I

These cases arise on appeals from two judgments of the District Court of the United States for the Western District of Pennsylvania. They involve the income and excess-profits tax liability of Diamond Alkali Company for the years 1918, 1919, and 1920. Nos. 4419 and 4426 are cross appeals from one of the judgments of the court below rendered with respect to the years 1918 and 1920. No. 4427 is an appeal by the defendant below from the judgment of the lower court for the year 1919. This petition is specifically addressed to Nos. 4419 and 4426 in so far as they relate to the income and profits tax liability of Diamond Alkali Company for the year 1918 and to No. 4427 in so far as it relates to the profits-tax liability for 1919. Since the decision of this court was so recently rendered, a

complete restatement of the facts and the questions of law involved would not seem necessary, and this petition is confined to the particular facts and questions of law relied upon in support of this request for rehearing.

II

The decision announced by the court in its opinion filed February 10, 1932, holds that although the net income of $3,821,134.63 found by the Commissioner of Internal Revenue should be reduced to $3,385,540.81 (a reduction of $435,593.82) the profits tax of $2,084,324.26 found by the commissioner may not be correspondingly reduced. In mathematical result this is equivalent to holding that the profits-tax rate of 54.54% found by the commissioner by means of special assessment should be increased to 61.59%. We believe that this court can scarcely have realized the anomaly of this outcome and the extraordinary results that follow from the principle employed. We believe and respectfully submit that the court has not construed sections 327 and 328 of the 1918 revenue act in accordance with the intent of Congress and prior decisions by the courts.

The effect of the decision

There was imposed, and the appellant paid, a profits tax amounting to 54.54% of the net income which the commissioner determined, as well as an income tax of 12% based on the same net income. The court has found that the net income was incorrectly computed by the commissioner, since the amortization deduction allowed by the commissioner was inadequate. It has allowed an additional deduction of $435,593.02 for the year 1918 on account of amortization of war facilities, thus reducing the taxable net income by $435,593.02. The income tax assessed upon this sum at 12% is some $52,270, which the court holds to be an overpayment. Applying to the same figure the profits-tax rate of 54.54% would indicate a similar overpayment on that account of some $237,572. Nevertheless the court by its decision holds the first to be recoverable but refuses to allow the second. It seems to us that the two must inevitably rise or fall together. In each case the tax must be predicated upon the taxpayer's true net income.

We do not believe that the special assessment provisions (relief provisions) of the 1918 act, or the decisions of the courts, wherein they have construed this statute, require this result. If the principle adopted by this court is sound, it may be applied generally. Let us suppose that this taxpayer had prevailed in its suit throughout and had obtained, as it claimed, an additional amortization deduction for 1918 amounting to $929,491.32 and an additional depreciation deduction of $439,104.16. Its net income then would have been $2,352,548.15. The profits tax, which this court has said may not be disturbed, amounts to considerably more than 80% of this net income. In other words, the principle employed by the court

would be tantamount to increasing the ratio of profits tax to true net income from 54.54% to more than 80%. It could hardly be said that relief results from the so-called relief provisions if they are to be so applied. On the actual facts of this case the court under the theory of not disturbing the commissioner's determination of special assessment has in effect increased the ratio of profits tax to net income from 54.54% to 61.59% of the correct net income. Has not the court redetermined the profits-tax rate by special assessment?

If the principle is sound, it should be susceptible of a further test. Suppose this taxpayer had by its suit shown errors in the net income as determined by the commissioner with the result that its correct net income was found to be only $2,000,000. Under the principle employed the fixed amount of profits tax then would be found to be more than 100% of the correct net income. And it would follow that if any taxpayer whose profits tax had been determined under special assessment should bring suit and should prove that by reason of losses not allowed by the commissioner it in fact had no net income, it would still be left under a large profits tax, although it had no net income, and this notwithstanding the fact that the statute imposes the profits tax upon net income alone.

These are logical results which might easily flow from an application of the principle adopted by the court.

Sections 327 and 328 provide a means for determining the rate of tax as distinguished from the tax itself

Like other taxes on net income the profits tax is the result of multiplying a net income by a rate. The special-assessment provisions are not used to determine the net income. The average net income of other comparative corporations is not used as a substitute for the taxpayer's net income; it is the taxpayer's own net income that is used. Nor do those provisions directly fix the tax. They specifically and solely provide a means of determining the ratio of net income that shall be taken as a tax; that is, they relate solely to a special means for arriving at a rate of profits tax. This rate, once determined by special assessment, must be applied to the correct net income.

We believe that the court has been led by false reasoning of the appellee to the conclusion that special assessment is the means of procuring the tax itself, instead of the rate which must then be applied to a net income before a tax is found. The error is fundamental and far-reaching.

The only case cited by the court and the case which it deemed to be controlling is Brown's Shamrock Linens, Ltd., v. Bowers (48 Fed. (2nd) 103). In that case the taxpayer admitted the correctness of the net income which the commissioner found and complained only of the rate. The taxpayer did not go before the court saying that an erroneous tax had been determined by special assessment, but that an

erroneous rate of taxation had been determined by that means. The court so viewed the issue, saying:

"Thus it is apparent that the complaint attacks the correctness of the ratio used by the commissioner and asks the court to review all the comparative data which under the statute must enter into his determination of such ratio."

The court then went on to say that on the authority of Williamsport Wire Rope Co. v. United States (277 U. S. 551) the majority of the court were of the opinion that the taxpayer's contention that the court review the comparatives must be denied.

In the case at bar the appellant abandoned its claim that the rate of 54.54% found by the commissioner was too high because improper comparatives had been used (the statement of claim having been filed before the Supreme Court's decision in the Williamsport Wire Rope case). The Government contended that the court was without jurisdiction to review the case at all and in reply the appellant contended that since the rate of 54.54% was not reviewable it should be applied to whatever net income the court might finally determine to be correct. But neither party presented argument leading to the result reached by the court.

We repeat that the factor which is here determined by the commissioner from the use of comparatives is the profits-tax rate and not the profits tax itself. The determination of the tax once the rate has been determined is merely a matter of mathematical computation. The process of performing this simple mathematical function is surely not one of discretion.

If net income is reduced the profits-tax rate may not be increased.

In the course of the oral argument of this case the Government handed up a typewritten reply brief, which was later printed and filed, in which it contended that the court should not take jurisdiction of the case, because if the commissioner should determine the profits-tax rate by special assessment on a reduced net income he might find a rate higher than 54.54%. This argument is wholly fallacious, and appellant has not heretofore had an opportunity to answer it specifically.

The profits tax provided by the statute is a graduated tax; that is, a part of the net income of 1918 is taxed at 30%, a certain excess is taxed at 65%, and a further excess, if any, is taxed at 80%. (1918 act, section 301.) Obviously if the net income is reduced to any extent that part falling in the 80% bracket will be lessened or eliminated, and if the reduction be sufficient that part falling in the 65% bracket will be lessened or eliminated. Therefore the inevitable effect under the statute of a reduction in net income is a reduction in the ratio of the total profits tax to the total net income.

A profits-tax rate determined from comparatives (by special assessment) must be derived from comparatives whose profits taxes

have been determined in the regular manner, that is, at graduated rates. (Section 328.) The statute provides for the selection of comparatives that are similarly circumstanced as to capital, net income, etc. The only change which this court was asked to make in 1918 or did make for 1918 was a reduction in net income. The abnormality on which the commissioner held that the taxpayer was entitled to special assessment was one of capital and not of income. (See offer of proof, B. E., p. 222.) If the commissioner had reduced this taxpayer's net income by $435,000 and had turned to other comparatives, it would not have been proper to employ comparatives whose invested capital was greatly less than those already used. Such new comparatives, if indeed new comparatives would seem necessary for a relatively small change in net income, would be comparatives with the same or approximately the same invested capital but with reduced net income. Necessarily the profits-tax rate so obtained could not exceed the 54.54% originally fixed and probably would be substantially less.

The Government's argument in the reply brief mentioned above is based on grossly distorted and improper illustrations of how a recomputation of the tax, after reduction of net income, might be made by special assessment. In each illustration, particularly in Nos. 1 and 2 (pp. 15, 16), forced results are obtained by methods that would undoubtedly amount to serious abuse of discretion if employed in actual practice. Plaintiff confidently asserts that the impropriety of the methods employed by way of illustration can be demonstrated if opportunity is afforded to it to file a brief and reargue the question.

The view taken by this court on the special-assessment issue was not suggested by either party to the litigation. It goes far beyond the requirements of the statute and the decision in Williamsport Wire Rope Company v. United States (277 U. S. 551). It means that if in any case special assessment be allowed, then, for the purposes of excess-profits taxes, determinations of taxable income by the commissioner, however erroneous, arbitrary, or invalid they may be, are not subject to any review or correction whatsoever. No argument has been offered directly upon the position taken by the court either in the briefs or at the bar. This question is so substantial both as to matter of law and the amount of tax involved that, we submit, briefs and oral argument upon it should be presented.

The foregoing applies likewise to the year 1919, No. 4427.

III

Another question is whether the taxpayer is entitled to depreciation for 1918 on the unamortized cost of depreciable assets; that is, whether the taxpayer is entitled to a deduction for depreciation on such part of the assets as remain after deducting the allowance for amortization. This question is decided by the court adversely to the taxpayer. Indeed the court not only declined to increase the

commissioner's allowance, but the court also disallowed a part of the depreciation allowed by the commissioner, namely, the depreciation on the limestone dock, which cost $340,000. Since the composite rate of depreciation was 10.4%, the court has reduced the depreciation allowance made by the commissioner by the sum of $35,360.

On the matter of deduction in 1918 for obsolescence of war facilities (obsolescence being one of the factors of so-called depreciation), the Supreme Court of the United States decided in favor of the taxpayer in the case of United States Cartridge Company v. United States. This decision was handed down by the Supreme Court on February 15, 1932, and is reported in the United States Daily of February 19, 1932. In that case the Supreme Court's construction of the statute relating to depreciation and amortization (subsections (7) and (8), section 234, revenue act of 1918) fully supports the appellant's contention and is contrary to the principle upon which this court necessarily proceeded in excluding depreciation on the entire cost of the limestone dock.

The court suggested in its opinion that the briefs did not point to facts in the record upon which a depreciation allowance could be made upon unamortized cost of war facilities. Since plaintiff was contending that amortization should be allowed on more facilities than the court below recognized, it was not feasible to burden otherwise lengthy briefs with various tabulations of specific facilities and their costs less amortization deductions. Appellant's briefs were prepared on the basis that once the court decided which facilities should be subject to amortization it would be a simple matter to compute unamortized costs of such facilities as the additional depreciation base. If the appellant is given opportunity to do so, it can readily set forth from the exhibits introduced the specific facilities and their unamortized costs which should be the basis for additional depreciation.

Wherefore, the appellant prays that this court will grant a rehearing in these causes.

JOHN W. DAVIS,
WILLIAM A. SEIFERT,
MAYNARD TEALL,
MARION N. FISHER,
Counsel for the Appellant, Diamond Alkali Company.

We, John W. Davis, William A. Seifert, Maynard Teall, and Marion N. Fisher, of counsel for the appellant, Diamond Alkali Company, do hereby certify that the foregoing petition for a rehearing of these causes is presented in good faith and not for delay.

JOHN W. DAVIS.
MARION N. FISHER.
WILLIAM A. SEIFERT.
MAYNARD TEALL.

In the United States Circuit Court of Appeals for the Third Circuit

No. 4419. October term, 1930

DIAMOND ALKALI CO., APPELLANT

vs.

D. B. HEINER, COLLECTOR, APPELLEE

Sur petition for rehearing

And now, to wit, April 5, 1932, after due consideration, the petition for rehearing in the above-entitled case is hereby granted.

Philadelphia.

J. W. THOMPSON, *Circuit Judge.*

[Endorsements:] 4419. Order granting petition for rehearing. Recd. & filed Apr. 5, 1932. Wm. P. Rowland, clerk.

In the United States Circuit Court of Appeals for the Third Circuit

No. 4426. October term, 1930

D. B. HEINER, COLLECTOR, APPELLANT

vs.

DIAMOND ALKALI CO., APPELLEE

Sur petition for rehearing

And now, to wit, April 5, 1932, after due consideration, the petition for rehearing in the above-entitled case is hereby granted.

Philadelphia.

J. W. THOMPSON, *Circuit Judge.*

[Endorsements:] 4426. Order granting petition for rehearing. Recd. & filed Apr. 5, 1932. Wm. P. Rowland, clerk.

In the United States Circuit Court of Appeals for the Third Circuit

No. 4419. October term, 1930

DIAMOND ALKALI CO., APPELLANT

vs.

D. B. HEINER, COLLECTOR, APPELLEE

No. 4426. October term, 1930

D. B. HEINER, COLLECTOR, APPELLANT

vs.

DIAMOND ALKALI CO., APPELLEE

And afterwards, to wit, 15th day of April, 1932, come the parties aforesaid by their counsel aforesaid, and this case being called for

reargument sur pleadings and briefs, before the honorable Joseph Buffington, honorable J. Warren Davis, and honorable J. Whitaker Thompson, circuit judges, and the court not being fully advised in the premises, takes further time for the consideration thereof,

And afterwards, to wit, on the 26th day of July, 1932, come the parties aforesaid by their counsel aforesaid, and the court, now being fully advised in the premises, renders the following decision:

In the United States Circuit Court of Appeals for the Third Circuit

No. 4419. March term, 1932

DIAMOND ALKALI COMPANY, A CORPORATION, PLAINTIFF-APPELLANT

v.

D. B. HEINER, COLLECTOR OF INTERNAL REVENUE FOR THE TWENTY-Third District of Pennsylvania, defendant-appellee

No. 4426. March term, 1932

D. B. HEINER, COLLECTOR, APPELLANT

v.

DIAMOND ALKALI COMPANY, APPELLEE

No. 4427. March term, 1932

C. G. LEWELLYN, FORMERLY COLLECTOR, APPELLANT

v.

DIAMOND ALKALI COMPANY, APPELLEE

Upon appeals from the District Court of the United States for the Western District of Pennsylvania

Opinion

Filed July 26, 1932

Before BUFFINGTON, DAVIS, and THOMPSON, Circuit Judges

DAVIS, Circuit Judge:

The Diamond Alkali Company filed a petition for rehearing on two points and seeks:

1. To have the tax rate of 54.54 per cent and 18.31 per cent, determined by the commissioner in a special assessment to be the fair and just rate for this corporation for 1918 and 1919, respectively, applied to its income as reduced by the decision of this court.

2. A deduction for depreciation on so much of its war facilities as were not amortized.

These questions will be considered in the above order.

1. The taxes for 1918 and 1919 are involved. The commissioner allowed a deduction for 1918 for amortization of war facilities of $315,956.89 and for 1919 a deduction of $71,267.51. But this court on reversing the redetermination of the Board of Tax Appeals allowed a deduction for 1918 of $790,187.16 and a deduction for 1919 of $175,838.94, making a total allowance for both years of $966,026.10 instead of $327,224.40 allowed by the commissioner. The net income of the petitioner, as determined by the commissioner, for 1918 was $3,921,143.63 and for 1919, $2,708,248.07. Applying the rate of 54.54 per cent to the income of 1918 as determined by him, the commissioner found that the company owed a profits tax of $2,084,324.26 for that year, and applying the rate of 18.31 per cent to the income for 1919 he found it owed a profits tax of $495,871.87 for that year.

The net income of the petitioner for the two years was reduced by our former decision by $578,801.70, yet the commissioner insists, and we held, that the total amount of the tax should not be reduced. If it is not reduced, it would result in a tax rate of 61.62 per cent for 1918 and a rate of 19.05 per cent for 1919 instead of 54.54 per cent and 18.31 per cent for those years, respectively, as fixed by the commissioner. This new rate would in effect be fixed by the court, which allowed deductions, but refused to apply the rate fixed by the commissioner to the reduced income. In other words, if the contention of the collector prevails, the petitioner will pay the same tax for the two years that it would have paid if its taxable income had not been reduced by $578,801.70. The collector contends that although the corporation's income was reduced more than one-half million dollars, its tax must nevertheless remain the same, for the reason that this court is without power to review the commissioner's determination of the taxpayer's liability for taxes, inasmuch as the taxes were determined by a special assessment.

The allowance or denial of a special assessment provided for in sections 327 and 328 of the revenue act of 1918 is an administrative question committed to the discretion or judgment of the Commissioner of Internal Revenue, subject, however, to review by the Board of Tax Appeals. Whether or not there are abnormal conditions affecting capital, as alleged in this case, or income which would work upon the corporation an exceptional hardship without the benefit of a special assessment; what are representative corporations to be used as comparatives, engaged in a like or similar trade or business; whether or not they are similarly circumstanced with respect to income, profits per unit of business transacted and capital employed the amount and rate of war profits or excess profits, and all other relevant facts and circumstances, are questions for the sole determination of the commissioner. (Blair v. Oesterlein Machine Company, 275 U. S. 220; Williamsport Wire and Rope Company v. United States, 277 U. S. 551, 559.) They have been committed by Congress to his judgment and discretion, which may not be exercised by the court. He has considered all these questions and in the light of all

the facts has determined rates which must be accepted by the court as fixed, fair, and just. In holding that the rates fixed by him shall be applied to the petitioner's true income, the court does not usurp the discretionary functions expressly conferred upon him.

The collector raises the objection that if the commissioner had not made a mistake in not allowing proper depreciation, other representative corporations might have been selected from which a different rate might have been fixed. This may or may not be true. It is purely suppositious. But when the commissioner applied these rates found and fixed by him as the proper ones to an improper income and thus unjustly increased the taxes of the petitioner, the court does have power to order that the proper rate be applied to the proper income, so that the taxpayer will pay only a proper and just tax. The power of the commissioner to determine an abnormality, to select representative corporations as comparatives, to allow a special assessment and fix the rate thereof, does not carry with it power so to fix the income on which the profits tax must be computed than an admittedly unjust amount of the tax is put beyond the review of the court. It is a bare possibility that the reduction of the income to the proper and just amount might have some conceivable effect on the selection of representative corporations. That was a matter for the commissioner, but when he found the correct rate, he could not apply it to an incorrect and false income and produce and unjust tax.

2. The second question is whether or not the taxpayer should have been allowed depreciation on so much of the war facilities as were not amortized.

The taxpayer's contention is tersely presented in the following statement:

1. Facilities based on production of soda ash:	
1917 cost less depreciation	$543,082.60
Amortization allowed, 49.803% of cost	270,473.60
Unamortized cost	$272,609.00
1918 cost	$1,002,144.35
Amortization allowed, 49.8034% of cost	499,101.96
Unamortized cost	$503,042.39
2. Boiler-house equipment:	
1917 cost	$56,583.88
Amortization, 15%	8,487.58
Unamortized cost	$48,096.30
1918 cost	$140,015.57
Amortization, 15%	21,002.34
Unamortized cost	$120,013.23
3. Flaking machine:	
1918 cost	$2,880.00
Amortization allowed	1,631.81
Unamortized cost	$1,248.19

4. Six tank cars:		
1918 cost		$23,655.00
Amortization allowed		13,402.92
Unamortized cost		$10,252.08
1917 unamortized costs on which depreciation at 10.4% is claimed:		
(1)	$272,609.00	
(2)	48,096.30	
	$320,705.30	
10.4% of above is	33,353.35	
1918 unamortized costs on which depreciation at 5.2% is claimed:		
(1)	$503,042.39	
(2)	129,013.23	
(3)	1,248.19	
(4)	10,252.08	
	$643,555.89	
5.2% of above is	33,464.91	

The commissioner did not allow any amortization on the limestone dock, which cost $340,000, but the District Court did allow amortization at the rate of 32 per cent, or a deduction of $108,800. This much of the cost of the limestone dock which has been allowed by way of amortization should not be included in the depreciation base, for the commissioner had already allowed depreciation at the rate of 10.4 per cent on the entire cost of $340,000. Therefore 10.4 per cent of the amortized cost should be deducted from any additional depreciation. This is 10.4 per cent of $108,800, or $11,315.20.

The total additional depreciation claimed by the taxpayer is therefore as follows:

10.4% of unamortized 1917 costs	$33,353.35
*5.2% of unamortized 1918 costs	33,464.91
	$66,818.26
Less 10.4% of $108,800, amortized cost of dock	11,315.20
Additional depreciation	$55,503.06

There is no contention, if we correctly understand the parties, that the above statement is not correct as to amounts and rate of depreciation, if depreciation is to be allowed in addition to allowance for amortization.

There is a question, however, as to whether or not amortization was intended to exclude depreciation for obsolescence or wear and tear. This is shown by the legislative history of the sections in question of the revenue act of 1918 (40 Stat. 1077), which controls this case. The Committee on Ways and Means, having charge of this measure, in its report said that many facilities provided for war purposes would be of little value after the end of the war; that under the law then existing it was impossible to allow deductions other than for "ordinary exhaustion, wear and tear, and depletion of such property" and that the purpose of the provision was "to allow spe-

cial amounts for amortization, according to the peculiar conditions in each case." (House Report 767, 65th Congress, 2d session, p. 10; Senate Report 617, 65th Congress, 3d session, p. 7.) It is thus evidence that the allowance for amortization was not intended to exclude allowance for depreciation on unamortized war facilities. This question is settled by the case of the United States Cartridge Company v. United States (284 U. S. 511, 516), where the Supreme Court in construing this provision said that "deductions for amortization were not intended to exclude obsolescence, but rather were to be made in addition or having regard to allowances deducted on account of obsolescence and the like."

The record, it seems to us, shows that the allowances made were for amortization only and not for depreciation for exhaustion, wear, tear, and obsolescence for the year 1918. The taxpayer is entitled to a deduction for depreciation for exhaustion, wear, tear, and obsolescence on its unamortized war facilities. No question has been raised as to the correctness of the composite rate of 10.4 per cent for depreciation for exhaustion, etc., on war facilities installed in 1917 and 5.2 per cent on those installed in 1918.

The order of the court is that the rates fixed by the commissioner for the years 1918 and 1919 will be applied to the reduced income and that the order of the District Court denying deductions for depreciation on unamortized war facilities is reversed.

Thompson, Circuit Judge, dissents.

A true copy. Teste:

_____,

Clerk of the United States Circuit Court of Appeals for the Third Circuit.

In the United States Circuit Court of Appeals for the Third Circuit

No. 4419 (List No. 48). October term, 1930

DIAMOND ALKALI COMPANY, APPELLANT

vs.

D. B. HEINER, COLLECTOR, APPELLEE

On appeal from the District Court of the United States for the Western District of Pennsylvania

This cause came on to be heard on the transcript of record from the District Court of the United States for the Western District of Pennsylvania and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this court that the judgment of the said District Court in this cause be, and the same is hereby, modified, with direction to the said District Court to enter a new judgment in accordance with the

opinion of this court, as further modified by the opinion of this court upon reargument in that the said District Court is directed to allow a deduction for depreciation on the unamortized portion of the war facilities, and is further directed to apply the rates fixed by the commissioner for 1918 to the reduced income as indicated by the two opinions of this court.

Philadelphia, July 26, 1932.

J. WARREN DAVIS, *Circuit Judge.*

[Endorsements:] 4419. Order modifying judgment, etc. Recd. & filed July 26, 1932. Wm. P. Rowland, clerk.

In the United States Circuit Court of Appeals for the Third Circuit

No. 4426 (List No. 49). October term, 1930

D. B. HEINER, COLLECTOR, APPELLANT

vs.

DIAMOND ALKALI CO., APPELLEE

On appeal from the District Court of the United States, for the Western District of Pennsylvania

This cause came on to be heard on the transcript of record from the District Court of the United States for the Western District of Pennsylvania and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this court that the judgment of the said District Court in this cause be, and the same is hereby, modified, with direction to the said District Court to enter a new judgment in accordance with the opinion of this court, as further modified by the opinion of this court upon reargument, in that the said District Court is directed to allow a deduction for depreciation on the unamortized portion of the war facilities, and is further directed to apply the rates fixed by the commissioner for 1918 to the reduced income as indicated by the two opinions of this court.

Philadelphia, July 26, 1932.

J. WARREN DAVIS, *Circuit Judge.*

[Endorsements:] 4426. Order modifying judgment, etc. Recd. & filed July 26, 1932. Wm. P. Rowland, clerk.

UNITED STATES OF AMERICA,
Eastern District of Pennsylvania,
Third Judicial Circuit, Set.:

I, William P. Rowland, clerk of the United States Circuit Court of Appeals for the Third Circuit, do hereby certify the foregoing to be

a true and faithful copy of the original transcript of record and proceedings in this court in the cases of (No. 4419) Diamond Alkali Co., appellant vs. D. B. Heiner, collector, appellee, (No. 4426) D. B. Heiner, collector, appellant, vs. Diamond Alkali Co., appellee, on file, and now remaining among the records of the said court, in my office.

In testimony whereof, I have hereunto subscribed my name and affixed the seal of the said court, at Philadelphia, this 19th day of October, in the year of our Lord one thousand nine hundred and thirty-two and of the independence of the United States the one hundred and fifty-seventh.

[SEAL.] WM. P. ROWLAND,
Clerk of the U. S. Circuit Court of Appeals, Third Circuit.

U. S. GOVERNMENT PRINTING OFFICE: 1932

1146 Supreme Court of the United States

No. 476, October term, 1932

Order allowing certiorari

Filed December 5, 1932

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

1147 Supreme Court of the United States

No. 477, October term, 1932

Order allowing certiorari

Filed December 5, 1932

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

1148 In Supreme Court of the United States

Nos. 476–478, October term, 1932

Stipulation as to printing of records for use on hearing of writs of certiorari

Filed Jan. 19, 1933

It is hereby stipulated by and between counsel for the parties to the above-entitled causes that, for the convenience of the court and in order to reduce the cost of printing the records for use on the hearing of the writs of certiorari granted in these causes, the clerk shall be required to print only the following portions of the printed records filed in connection with the submission of the petition for certiorari:

1149 I. Record Nos. 4419 and 4426, Circuit Court of Appeals

(1) Page 1 to paragraph 10, page 7.
(2) Page 7, paragraph 11, to page 15, paragraph 33.

(3) Page 17, paragraph 40, to page 23, paragraph 10.

(4) Page 24, paragraph 11, to page 39, paragraph 36.

(5) Page 41, paragraph 40, to page 44, "Third separate defense."

(6) Page 45, beginning "Wherefore, the defendant, having fully answered," etc., to page 57.

(7) Page 64, beginning "Plaintiff's reply," to page 75, paragraph 37.

(8) Page 76, beginning "Defendant's first separate defense," to page 77, "Defendant's third separate defense."

(9) Page 78, signature of attorneys for the plaintiff, to page 84, paragraph commencing with the words "By striking out paragraph 10," etc.

(10) Page 84, beginning with the words "By striking out paragraph 11," etc., to page 87, paragraph 9 (a).

(11) Page 90, subparagraph (b), to page 92, paragraph 42.

(12) Page 93, signatures of attorneys for plaintiff, to page 95, paragraph IX.

(13) Page 95, beginning with the words "Answering the allegations contained in paragraph 9 (b)," etc., to page 97, paragraph X.

(14) Page 98, paragraph XI, to page 100, paragraph beginning with the words "And as a further and separate defense," etc.

(15) Page 100, signature of defendant, to page 109, paragraph fourth.

1150 (16) Page 115, paragraph sixth, to page 117, paragraph eighth.

(17) Page 120, paragraph seventeenth, to page 131, paragraph ninth.

(18) Page 141, paragraph 54, to page 142, paragraph 56.

(19) Page 163, beginning with paragraph "Wherefore defendant prays," etc. to and including page 194.

II. Bill of exceptions Nos. 4419 and 4426

1. Vol. I:

(a) Page 1 to page 5, beginning with the words "Mr. Teall."

(b) Page 30, beginning with the words "Testimony of Thomas R. Evans," to page 31, beginning with the words "Q. What is the original substance from which these others are derived?"

(c) Page 42, beginning with the words "Q. It appears in the pleadings," etc., to page 44, beginning with the words "Q. Now Mr. Evans, when was your company organized?"

(d) Page 221, beginning with the words "Testimony of A. G. Wallerstedt," to page 223, "Defendants' testimony."

(e) Page 322, beginning with the words "Mr. Teall," to and including page 324.

2. Vol. II:

(a) Plaintiff's Exhibit No. 1, pages 325–330.

(b) Plaintiff's Exhibit No. 4, pages 354–371, including notice.
(c) Plaintiff's Exhibit No. 5, pages 372–383.
(d) Defendant's Exhibit Z, pages 576–587.
(e) Page 768.

3. Vol. III:

(a) Page 1020.
(b) Pages 1072–1117, inclusive.

1151 III. Record No. 4427

(1) Page 1 to page 55, "Plaintiff's request for findings of fact."
(2) Page 69 to page 88, paragraph 7.
(3) Page 107, paragraph 70, to and including page 136.

The parties hereby stipulate that either shall have the right to refer in their briefs and oral arguments to any portions of the records in these causes as filed in this Court on petition for certiorari which are not contained in the records as printed pursuant to this stipulation.

THOMAS D. THACHER,
Solicitor General.
MARION N. FISHER,
Counsel for Respondent.

JANUARY 18, 1933.

(File endorsement omitted.)

U. S. GOVERNMENT PRINTING OFFICE: 1933

(No. 5762 law) this court should find that said claims for depreciation should be allowed, it follows that plaintiff's invested capital for the year 1919 should be reduced in a corresponding amount, with consequent increase in plaintiff's tax liability for the said year.

27. If plaintiff's said claim for additional deductions from its gross income for 1918 in said action, namely, law No. 5762 (and for 1919 in this action) are allowed on account of amortization of war-time facilities and depreciation of capital assets, and plaintiff's profits tax is computed under section 301 of the revenue act of 1918, the adjustment thereby resulting will increase the total income and profits taxes due (and unpaid) from this plaintiff for the year 1919 in an amount greatly in excess of the sum sought to be recovered in this action.

28. A true statement of plaintiff's gains, profit, income, and invested capital for the year 1919, showing its tax liability, after its said claims for additional deductions from its 1918 and 1919 gross incomes on account of amortization and depreciation shall have been allowed and its excess profits tax for 1919, shall have been computed under section 301 of the revenue act of 1918, is as follows:

NET INCOME

Net income disclosed by bureau letter dated July 11, 1927		$2,708,248.07
Addition:		
(a) Depreciation disallowed on account of revision in amortization allowance for 1918		134,661.40
Total		$2,842,909.47
Deduction:		
(b) Additional amortization allowed		27,749.01
Net income as corrected		$2,815,160.46

INVESTED CAPITAL

Invested capital as shown by the revenue agent's report dated July 31, 1922		$7,074,164.11
Additions:		
(a) Profit on sale of dock, 1917	$6,426.45	
(b) Obsolescence disallowed 1918	150,279.59	
(c) Income tax, prior years	160,409.45	
Total additions		317,115.49
		$7,391,279.60
Deductions:		
(d) Income tax, 1918	$6,944.01	
(e) Miscellaneous revenue reserves	62,908.97	
(f) Loss on sale of locomotive 1917	10,000.00	
(g) Paid-in surplus (contracts)	1,275,000.00	
(h) Amortization 1918	90,021.00	
(i) Inadmissible assets	2,195.23	
Total deductions		1,447,069.21
Invested capital as adjusted		$5,944,210.39

PROOF OF INVESTED CAPITAL

Capital stock		$2,163,500.00
Surplus amended		4,001,068.08
Reserves		392,996.34
Premium on sale of stock		20,000.00
Capital surplus (Harbor Land Co.)		464.36
Total, as corrected, beginning of year		$7,028,028.78
Addition:		
Sale of capital stock ($10,000.00 effective 50 days)		1,369.86
Total		$7,029,398.64
Reductions:		
Income tax (1918)	$685,487.28	
Additional income tax prior years	275,857.80	
Dividends paid Jan. 15, 1919 ($126,500.00)	121,647.94	
Inadmissibles	2,195.23	
Total reductions		1,085,188.25
As shown above		$5,944,210.39

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COMPUTATION OF TAX

Excess Profits Tax:	
Net income	$2,815,160.46
Invested capital	$5,944,210.39
8% of invested capital	$475,536.83
Exemption	$3,000.00
Total credit	$478,536.83

	Income	Credit	Balance	Rate	Profits tax
20%	$1,118,842.08	$478,536.83	$710,305.25	20%	$142,061.05
Balance	1,626,318.38		1,626,318.38	40%	650,527.35
Totals	$2,815,160.46	$478,536.83	$2,336,623.63		$792,588.40

Amount brought forward (Profits tax)			$792,588.40
Income tax:			
Net income		$2,815,160.46	
Less:			
Interest on U. S. obligations not exempt	$69,981.11		
Profits tax	792,588.40		
Exemption	2,000.00		
		864,569.51	
Balance taxable at 10%		$1,950,590.95	195,059.10
Total profits and income tax			$987,647.50
Less:			
Tax previously paid			709,911.38
Balance due and owing			$277,736.12

33 29. Wherefore, defendant, having fully answered, demands that he have judgment in his favor and that he go hence with his costs in this behalf expended.

C. G. LEWELLYN, *Defendant.*
JOHN D. MEYER,
United States Attorney for the Western District of Pennsylvania,
JOHN A. MCCANN,
Special Assistant to the U. S. Attorney,
Attorneys for the Defendant.

Duly sworn to by C. G. Lewellyn. Jurat omitted in printing.

34 In United States District Court

Plaintiff's reply

Filed Jan. 14, 1929

And now comes the Diamond Alkali Company, a corporation, the above-named plaintiff, and replies as follows to the new matter alleged in defendant's affidavit of defense:

6. Plaintiff admits that its tax liability for 1918, 1919, and 1920, except as to the plaintiff's allowance for amortization of war-time facilities, was in process of audit by the Commissioner of Internal Revenue to on or about July 11, 1927, but denies that such process of audit began when plaintiff's returns were filed or was continuous, and avers on information and belief that said audit began several months subsequent to the respective dates on which plaintiff's returns were filed and was alternately ceased and resumed thereafter with decisions by the commissioner from time to time to which the plaintiff objected and which were changed by the commissioner in divers particulars. Plaintiff denies the averment, as such averment is made in the affidavit of defense, that said letter of July 11, 1927, stated only the final adjustments, and avers that said letter was the commissioner's usual form of communication provided for by section 274 (a) of the revenue act of 1926 and variously called deficiency letter, sixty-day letter, or notice of deficiency. Plaintiff denies that its said amortization allowance was ever, or was ever capable of being, the subject of audit, and avers that said allowance was an engineering and not an auditing or accounting matter, that the
35 commissioner's auditors and accountants had no skill or expert knowledge or information thereof, and in respect to that particular deduction from gross income, as plaintiff avers on information and belief, were authorized and directed to accept the determination of the amortization section of the Income Tax Unit of the Bureau of Internal Revenue and to compute the tax liability, so far as the same depended on the amortization allowance, upon the

basis of such determination. Plaintiff avers that its said amortization allowance was determined by said amortization section on or about December 2, 1921, at $1,344,465.15, of which $1,245,448.21 was a deduction from gross income for 1918 and $99,016.94 a deduction from gross income for 1919, that such determination was accepted by the plaintiff and was never the subject of audit, that said determination was unquestioned by either the plaintiff or the commissioner until on or about October 1, 1924, that on or about October 1, 1924, the plaintiff's said allowance was assigned for reinvestigation, that such reinvestigation did not begin until on or about April 1, 1925, and that subsequent to April 1, 1925, two successive attempted redeterminations of plaintiff's said allowance were made as described in the statement of claim. Said letter of July 11, 1927, incorporated the plaintiff's said allowance as fixed or attempted to be fixed by said second attempted redetermination.

7. Plaintiff denies that said alleged determination at $387,224.40 was the only determination of plaintiff's amortization allowance made by the Commissioner of Internal Revenue, and avers
36 that one previous determination and one previous attempted redetermination thereof were made by the said commissioner as alleged in the statement of claim.

Plaintiff denies that said allowance was determined only once as alleged in the affidavit of defense, and avers that one previous determination and one previous attempted redetermination were made by the commissioner or under his authority, as alleged in the statement of claim, and that the only determination made prior to March 3, 1924, was said determination at $1,344,465.15 made on or about December 2, 1921.

8. Plaintiff denies that its correct tax liability for 1919 was $709,911.38, and avers that its correct tax liability for said year was $702,571.12.

9. Plaintiff denies that the function of said amortization section was only to make investigations, examinations, and recommendations as to the allowance of amortization claims, or that said claims, when approved by the chief or acting chief of said amortization section and notified to the taxpayer, were subject to further audit or review by the Bureau of Internal Revenue, and avers that an allowance approved by the chief or acting chief of the amortization section as described in the statement of claim was a final determination by the commissioner as to amortization allowance.

10. Plaintiff denies on information and belief that said
37 chief or acting chief had no power or authority to determine the amount of such allowance, and while admitting that the power to determine such allowance was vested in the Commissioner of Internal Revenue, avers that the said commissioner acts and at all times has acted through his subordinates, is not and never has been able to make such determinations personally, and avers on information and belief that the chief or acting chief of said amor-

tization section had full power and authority to make determinations of amortization allowances as alleged in paragraph 9 of the statement of claim. Plaintiff denies that said chief or acting chief made merely a report or recommendation that was subject to further audit and review, and avers on information and belief that said chief or acting chief made and was authorized to make final determination of amortization allowances. Plaintiff denies that amortization allowances could not be made or become final without the approval of the commissioner personally or of the assistant to the commissioner, and avers on information and belief that as a matter of practice, well known to and acquiesced in by the commissioner, all final determinations of amortization allowances were made by the chief or acting chief of said amortization section and were notified as such to taxpayers, and that the action by such acting chief, as set out in the statement of claim, was a final determination of the plaintiff's amortization allowance.

11. Plaintiff admits that the sole power of said Griffith was to investigate and make written report to said amortization sec-
38 tion, but avers that his said report was a determination, and on approval by said B. L. Wheeler, chief of engineers, and approval by said T. J. S. Kishpaugh, acting chief of said amortization section, as described in the statement of claim, became and was a final determination of the plaintiff's amortization allowance.

12. Plaintiff admits that said Griffith's report to said amortization section constituted only a recommendation, but avers that the approval thereof by said B. L. Wheeler, chief of engineers, and said T. J. S. Kishpaugh, acting chief of said amortization section, as described in the statement of claim, constituted a final determination of the plaintiff's amortization allowance at the sum of $1,344,465.15, and that $99,016.94 thereof was deductible from 1919 gross income.

13. Plaintiff admits that said Griffith's report to said amortization section was a mere recommendation, but denies that the action of said B. L. Wheeler was a mere approval of a recommendation, and avers that the action of B. L. Wheeler, chief of engineers, and said T. J. S. Kishpaugh, acting chief of said amortization section, as described in the statement of claim, constituted a final determination of plaintiff's amortization allowance and was notified to the plaintiff as such.

14. Plaintiff denies that said report, when approved by said Wheeler and said Kishpaugh as described in the statement of claim was a mere recommendation or that the action of said Kish-
39 paugh was a mere concurrence in a recommendation previously made, or that the action of said Kishpaugh was subject to further audit or review, and avers on the contrary that the said report, when approved by said Wheeler and said Kishpaugh as described in the statement of claim, became and was a final determination of the plaintiff's amortization allowance. Plaintiff denies on information and belief that said Kishpaugh was without authority to make a

final determination, and avers on information and belief that said Kishpaugh, as acting chief of said amortization section, was fully authorized in the premises.

15. Plaintiff denies that its said expression of willingness to accept said determination in the sum of $1,344,465.15 was conditioned on the closing of its case, and avers that said final determination was notified to the plaintiff as described in the statement of claim and was accepted by the plaintiff without further objection and without any condition whatsoever upon the plaintiff's acceptance. Plaintiff denies that said report appears on its face or otherwise to be a mere recommendation, denies that the same was subject to further audit, denies that the plaintiff was advised at the time of delivery or at any other time that the same was only a recommendation, and avers that said report, when approved as described in the statement of claim, became and was a final determination of the plaintiff's amortization allowance and was notified to and accepted by the plaintiff as such.

16. Plaintiff denies that in briefs or otherwise it requested
40 further adjustments in its said amortization allowance as determined at $1,344,465.15, and avers that its said briefs had express reference to the commissioner's subsequent alleged redeterminations and contained protests against the same. Plaintiff denies that the first reexamination of said return with respect to said allowance was begun in 1921 and had not been completed on March 3, 1924, and was not completed until several years thereafter, and avers on the contrary that prior to March 3, 1924, the commissioner made final determination of the plaintiff's amortization allowance at $1,344,465.15 as alleged in the statement of claim, and subsequent to March 3, 1924, instituted new reexaminations and attempted to make new determinations. Plaintiff denies that its amortization allowance was never determined at $1,344,465.15, and avers that it said allowance was determined at $1,344,465.15, as averred in the statement of claim. Plaintiff denies that its said claim for amortization allowance was from the year 1921 to a long time subsequent to March 3, 1924, in process of audit or investigation or consideration, and avers that after the final determination of the plaintiff's amortization allowance by said T. J. S. Kishpaugh, as described in the statement of claim until on or about October 1, 1924, no further proceedings were had or taken with respect to plaintiff's amortization allowance and that on or about October 1, 1924, a new examination was ordered, which, however, was not begun until on or about April 1, 1925. Plaintiff avers that the commissioner's original determination and his two subsequent attempted redeterminations were successive, and denies that the commissioner's attempted
41 action in respect to plaintiff's amortization allowance had the element of continuity. Plaintiff denies that its said claim was continuously in process of audit and avers that a final determination was made by said T. J. S. Kishpaugh, acting chief of said amortization section, who acted on behalf of the Commissioner of Internal

Revenue, on or about the 10th day of January, 1922. Plaintiff denies that no determination was made until approval of the allowance by the assistant to the commissioner on or about July 11, 1927, and avers that a final determination was made on or about the 2d day of December, 1921, and that said two subsequent attempted determinations were, as stated in their titles, attempted redeterminations.

17. Plaintiff denies that said further examination was a continuance of any examination or audit theretofore begun, and avers that the same was a new examination. Plaintiff denies that there was only one examination or investigation of the plaintiff's return, which was commenced prior to March 3, 1924, and ended subsequent thereto, and avers that plaintiff's amortization allowance was determined on or about December 2, 1921, as aforesaid, and that the attempted subsequent redeterminations were de novo. Plaintiff denies that said report of Luce was a mere recommendation subject to further review, or appears to be such on its face, and avers that the same was sent and noticed to the plaintiff as an attempted redetermination.

18. Plaintiff denies that said paper entitled "Second Redetermination of Amortization Claim" was a mere recommendation, or was subject to further review, or appeared on its face to be subject to further review, and avers on information and belief that when the same was approved by M. W. Nolan, reviewing engineer, and one Stack, chief of said amortization section, as in fact it was approved, it became and was an attempted redetermination of the plaintiff's amortization allowance.

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19. Plaintiff denies that it was entitled to an amortization deduction of only $71,267.51 for 1919, and avers that it was and is entitled in law and in fact to an amortization deduction from gross income of 1919 in the sum of $99,016.94.

20. Plaintiff denies that only one determination or attempted determination was made, and avers that its amortization allowance was determined at $1,344,465.15 on or about December 2, 1921, and that subsequent to April 1, 1925, two new and subsequent attempted determinations or redeterminations were made as described in the statement of claim. Plaintiff admits that the commissioner undertook or attempted to make a determination of its amortization allowance at $387,224.40, of which $71,267.51 was a deduction from gross income for 1919, but avers that such attempted determination was an attempted redetermination after expiration of the stautory period of limitation therefor and was void and of no effect. Plaintiff denies that said reports were mere recommendations and avers that when the same were approved by the chief or acting chief of said amortization section they became and were determinations by the commissioner. Plaintiff denies that said two subsequent attempted determinations were based on new or additional evidence, except plaintiff admits that said Luce's examination was subsequent to said Griffith's and therefore included observation of production at plaintiff's plant over a period of time not yet elapsed when said Griffith's examination was made. Plaintiff admits that

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said Griffith erred in his report to the extent that he did not allow plaintiff's claim of $1,756,453.64 in full but denies other errors as alleged by defendant and avers that said Griffith's report was otherwise correct in amount of the allowance as approved by said acting chief of said amortization section. Plaintiff denies that said Griffith's report was based on the assumed fact that several plant units of the plaintiff were no longer required by plaintiff in the operation of its business whereas the truth was that said plant units were only temporarily idle at the time of said Griffith's examination and were in fact required by the plaintiff, and avers that the report of said Griffith was not predicated on disused plant units, but on the ratio of post-war needs or requirements of plant to entire plant available. Plaintiff admits that said Griffith's investigation and report were made during a period of temporary business depression, but denies that said fact prevented the said Griffith from ascertaining the plaintiff's plant requirements during the post-war period. Plaintiff denies that it was discovered on subsequent investigation or otherwise that the cost upon which said Griffith had recommended amortization was in excess of the true cost, and avers that, on the
44 contrary, neither of said subsequent attempted redeterminations indicated any error in the costs upon which the amortization was claimed. Plaintiff avers that said two subsequent attempted redeterminations were erroneous in fact and void in law.

21. Plaintiff admits that the sum specified in said claim was $45,000.00, but avers that a claim for refund of $45,000.00 includes a claim for refund of $8,807.90. Plaintiff avers that the reasons for refund specifically set out in said claim were as stated by the defendant. Plaintiff avers that when said claim for refund was filed, to wit, March 11, 1925, said determination of its amortization allowance at $1,344,465.15 had previously been made, that plaintiff had received no notice or suggestion that any examination or reexamination was contemplated by the commissioner, and that in fact no reexamination had yet been begun, and neither of said two subsequent attempted determinations had yet been made. Plaintiff accepted the said amortization determination of $1,344,465.15 and for that reason did not make protest in its claim for refund in the matter of amortization.

DEFENDANT'S FIRST SEPARATE DEFENSE

23. Plaintiff denies the averments of paragraph 23 and avers that the court has full jurisdiction in the premises.

24. Plaintiff denies the averments of paragraph 24.

45 DEFENDANT'S SECOND SEPARATE DEFENSE

25. Plaintiff denies the conclusion of law that if the court shall find the commissioner's determination of the plaintiff's tax liability

puted under section 301 of the revenue act of 1918, avers that the in any way erroneous, then the plaintiff's tax for 1919 must be computed abnormalities upon which relief was granted under said sections 327 and 328 were abnormalities of capital, and avers that alterations of the plaintiff's capital or income by decisions of this court will leave unaffected the plaintiff's right, already acknowledged of record by the Commissioner of Internal Revenue, to have its excess profits tax for 1919 computed under the provisions of said sections 327 and 328.

26. Plaintiff denies that its said amortization claim for $1,756,453.64 was disallowed in the sum of $1,369,229.24 and allowed in the sum of $387,224.40, and avers that the plaintiff's amortization allowance was determined by the commissioner at $1,344,465.15 on or about December 2, 1921, as aforesaid, and that subsequent to April 1, 1925, the commissioner undertook or attempted to make two successive and different redeterminations of said allowance as hereinabove described. Plaintiff denies that there is or will be any necessity for any computation or recomputation or reduction of its invested capital, and avers that the abnormalities on which the Commissioner of Internal Revenue has heretofore granted special assessment under sections 327 and 328 of the revenue act of 1918 are abnormali-
46 ties of capital and will remain wholly unaffected by any change in income, and that when the tax is computed under said sections the plaintiff's invested capital is immaterial, for the computation is by a percentage of income and without reference to invested capital of the plaintiff.

27. Plaintiff does not deny the averments of paragraph 27 of the affidavit of defense, but does deny that there is or ever will be any reason or necessity or right to compute its tax under said section 301.

28. Plaintiff denies that said computation set out in paragraph 28 of the affidavit of defense is correct, and avers that the correct computation of plaintiff's tax liability under said section 301, if plaintiff's tax could lawfully be computed under said section, is shown in Exhibit A hereto attached and hereby made a part hereof.

SMITH, SHAW & MCCLAY,
Attorneys for the Plaintiff.

Duly sworn to by W. E. Jones; jurat omitted in printing.

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Exhibit A to reply

1919

Net income		$2,680,498.64
Invested capital		6,371,733.99
Excess profits tax credit		512,740.32
Excess profits tax:		
Exemption	$512,740.32	
Taxable @ 20%	961,610.48–$192,322.10	
Taxable @ 40%	1,206,147.84– 482,459.14	
Total	2,680,498.64	674,781.24

Income tax:			
Net income		$2,680,498.64	
Exempt int	$69,981.11		
Ex. profits tax	674,781.24		
Exemption	2,000.00		
		746,762.35	
Taxable @ 10%		1,933,736.29	$193,373.63
Total tax			868,154.87

48 In United States District Court

Amendment to statement of claim

Filed Feb. 14, 1930

Diamond Alkali Company, by leave of court first had and obtained, amends its statement of claim heretofore filed to agree with the findings of fact of the trial court filed February 10, 1920, as follows:

1. The introduction is amended to read as follows:

"Diamond Alkali Company, the above-named plaintiff, has a claim against C. G. Lewellyn, formerly collector of internal revenue for the twenty-third district of Pennsylvania, defendant, for the sum of $13,106.40, with interest thereon from the 15th day of December, 1920, upon a cause of action whereof the following is a statement."

2. Paragraph 5 is amended to read as follows:

"5. Only $696,804.98 of said tax of $711,379.02 was in fact owing and $14,574.04 thereof was an overpayment. Said overpayment was made by plaintiff to defendant on or about December 15, 1920. $1,467.64 thereof has been allowed to plaintiff as a credit on alleged additional taxes for 1918, leaving a net overpayment of $13,106.40."

3. Paragraph 7 is amended to read as follows:

"7. The change and adjustment which resulted in alleged overpayment of $1,467.64 instead of the correct amount of overpayment, $14,574.04, was as follows: Redetermination of the plaintiff's
49 allowance for the amortization of war-time facilities under section 234 (a) (8) of the revenue act of 1918 in the sum of $387,224.40 instead of permitting the same to stand at $1,344,465.15 as determined at the time and in the manner hereinafter described, whereby the plaintiff's deduction from 1919 gross income on account of said allowance was changed from $99,016.94 to $71,267.51."

4. Paragraph 8 is amended to read as follows:

"8. Said tax of $711,397.02 and the assessment and collection thereof were and are erroneous, illegal, and void to the extent of $14,574.04. Annexed hereto, marked 'Exhibit 1,' and made part hereof is a correct statement of the plaintiff's income and profits tax liability for the year 1919, showing the amount actually owing, the amount the plaintiff was compelled to pay, and the amount of tax paid by plaintiff in excess of the amount owing and for the recovery of which this suit is brought."

5. Paragraph 21 is amended to read as follows:

"21. On or about the 11th day of March, 1925, the plaintiff filed with the commissioner, on the form prescribed by him for that purpose, claim for refund of said overpayment of tax in the sum of $8,807.90, or such greater amount as is legally refundable, on the ground that said tax and the assessment and collection thereof were erroneous, illegal, and void to the extent of said overpayment, but on or about July 11, 1927, the commissioner rejected said claim except $1,467.64 thereof."

50 6. Paragraph 22 is stricken out and a new paragraph inserted to read as follows:

"22. The reasonable deduction to which plaintiff is entitled on account of amortization of plantiff's war-time facilities is $120,793.24."

7. Paragraph 23 is inserted to read as follows:

"23. Except for $1,467.64, no part of said overpayment of $14,574.04 has been repaid or refunded to the plaintiff."

8. The ad damnum clause is amended to read as follows:

Wherefore, this suit is brought and plaintiff claims judgment against the defendant for the sum of $13,106.40, with interest thereon from the 15th day of December, 1920.

SMITH, SHAW, MCCLAY & SEIFERT,
Attorneys for Plaintiff.

Duly sworn to by W. E. Jones, jurat omitted in printing.

51 EXHIBIT 1 TO AMENDMENT

SCHEDULE

1919 taxes

Net income		$2,708,248.07
Less additional amortization		49,525.73
		2,658,722.34
Excess profits tax at 18.31% of net income as determined by commissioner		486,812.06
Income tax:		
Income		2,658,722.34
Less:		
Liberty bond interest	$69,981.11	
Excess profits tax	486,812.06	
Specific exemption	2,000.00	558,793.17
Taxable at 10%		2,099,929.17
52 Tax liability: OR		209,992.92
Excess profits tax		486,812.06
Taxable at 10%		209,992.92
Total tax liability		696,804.98
Tax paid with return		711,379.02
Correct tax liability		696,804.98
Tax overpaid		14,574.04
Overpayment credited		1,467.64
		13,106.40

In United States District Court

**Bill of Exceptions*

Stipulation as to bill of exceptions

And now, to wit, May 27, 1930, it is hereby stipulated and agreed by and between the parties hereto, acting by their respective attorneys, that the following matter contained in plaintiff's bill of exceptions as printed at No. 5762 law:

Stipulation waiving jury trial,
Transcript of testimony,
Defendant's request for findings of fact,

together with the following matter contained in the proceedings at No. 5761 law, to wit:

Motion for judgment for plaintiff,
Motion for judgment for defendant,
Plaintiff's request for findings of fact,
53 Opinion, findings of fact and conclusions of law, and order for judgment,
Motion to vacate judgment and order,

shall be, and hereby is, regarded as defendant's bill of exceptions in defendant's appeal in the above-entitled case, and that the same be settled and allowed by the court without further notice.

SMITH, SHAW, MCCLAY & SEIFERT,
Attorneys for the Plaintiff.

LOUIS E. GRAHAM, *U. S. Attorney,*
W. J. AIKEN, *Ass't U. S. Attorney,*
Attorneys for the Defendant.

Order

And now, to wit, May 27, 1930, it is ordered that in pursuance of the foregoing stipulation entered into by and between the respective counsel for plaintiff and defendant, that the following matter contained in the bill of exceptions heretofore allowed, settled, signed, sealed and ordered filed as the plaintiff's bill of exceptions at No. 5762 law, to wit:

Stipulation waiving jury trial,
Transcript of testimony,
All exhibits,
Defendant's request for findings of fact,

together with the following matter contained in the proceedings at No. 5761 law, to wit:

54 Motion for judgment for plaintiff,
Motion for judgment for defendant,
Plaintiff's request for findings of fact,

Opinion, findings of fact and conclusions of law, and order for judgment,

Motion to vacate judgment and order,

be, and hereby is, allowed, settled, signed, sealed, and ordered filed as defendant's bill of exceptions in the above-entitled case, this order being made and entered into within the period in which an appeal may lie from the final judgment entered herein on the 14th day of February, 1930, and within the order of court extending to the defendant time for filing bill of exceptions until May 28, 1930.

R. M. GIBSON,
Judge of the District Court of the United States for the Western District of Pennsylvania.

Motion for judgment for plaintiff

And now, January 23rd, 1929, comes counsel for plaintiff and moves the court that under the pleadings and all of the evidence in this case, judgment must be entered for the plaintiff for the full amount of its claim.

JOHN W. DAVIS,
SMITH, SHAW, MCCLAY & SEIFERT,
Attorneys for Plaintiff.

55 *Motion for judgment for defendant*

Comes now the defendant, C. G. Lewellyn, by his attorneys, John D. Meyer, United States attorney for the western district of Pennsylvania, and John A. McCann, special assistant to the United States attorney, and moves the court for judgment in his favor and for his costs on the ground that the pleadings and the evidence are insufficient to support a judgment in favor of the plaintiff.

JOHN D. MEYER,
United States Attorney for the Western District of Pennsylvania.

JOHN A. MCCANN,
Special Assistant to the U. S. Attorney,
Attorneys for the Defendant.

56-68 [Omitted.]

69 In United States District Court

Opinion

Filed Feb. 10, 1930

GIBSON, District Judge.

This suit has been brought by the plaintiff against the defendant to recover alleged overpayments of 1919 taxes which were made over

protest and pursuant to threats of distraint. A jury trial was waived. From the testimony introduced we make the following

FINDINGS OF FACT

1. Diamond Alkali Company, the plaintiff, is, and at all times material herein was, a West Virginia corporation with its manufacturing plant at Painesville, Ohio, and its principal administrative office in the city of Pittsburgh, Pennsylvania.

2. C. G. Lewellyn, the defendant, at the date when the moneys herein sued for were paid, was the duly appointed, qualified, and acting collector of internal revenue for the 23rd district of Pennsylvania. Said defendant resides in the city of Pittsburgh and within the western district of Pennsylvania.

3. For the year 1919 the plaintiff kept its books of account on on the accrual basis and filed its Federal income and profits tax returns on the accrual and calendar year basis.

4. The plaintiff filed its return for 1919 on May 12, 1920.
70 The said return for 1919 showed income and profits taxes of $711,392.02, which sum was duly paid by the plaintiff to the defendant.

5. By letter dated July 11, 1927, the Commissioner of Internal Revenue (hereinafter called the "commissioner"), notified the plaintiff that its income and profits tax return for the year 1919 was erroneous; that he, the commissioner, had made divers changes and adjustments in the return and in the figures upon which the taxes thereby indicated were computed; and that as a result of such changes and adjustments, plaintiff had overpaid its taxes for the said year 1919 by the sum of $1,467.64.

6. On or about March 11, 1925, the plaintiff filed with the commissioner, on the form prescribed by him for that purpose, claim for refund of $45,000.00 of 1919 taxes theretofore paid by the plaintiff.

7. The sum of $8,807.90 claimed by the plaintiff in this proceeding to have been overpaid, the same being a part of the said sum of $711,379.02, was paid by the plaintiff to this defendant on December 15, 1920.

8. The aforesaid sum of $1,467.64 found by the commissioner to have been an overpayment, has never been refunded or paid to the plaintiff, but the same was applied or credited on or about November 7, 1927, by the defendant's successor in office against alleged additional taxes for 1918.

9. On or about November 7, 1927, the defendant's said suc-
71 cessor served upon the plaintiff written notice of assessments of alleged additional taxes for 1918 and 1920 greatly in excess of $1,467.64, and demand for payment thereof. Said notice gave credit of $1,467.64 on said alleged additional taxes for 1918.

10. The change and adjustment which resulted in the alleged overpayment of $1,467.64 instead of $8,807.90 was the commissioner's redetermination of plaintiff's deduction for the amortization of wartime facilities under section 234 (a) (8) of the revenue act of 1918, in the sum of $387,224.40, instead of permitting the same to stand at $1,344,465.15 as previously determined by the commissioner on or about December 1, 1921, whereby the plaintiff's deduction from its gross income for 1919 on account of the said amortization of wartime facilities was reduced from $99,016.94 to $71,267.51.

11. The plaintiff constructed, erected, installed, and acquired between April 6, 1917, and March 31, 1919, inclusive, certain buildings, machinery, equipment, and other facilities for the production of articles contributing to the prosecution of the war with Germany. The cost of these facilities to the plaintiff after depreciating to January 1, 1918, those facilities which were installed during 1917, was $2,195,096.42.

12. A schedule of all of the aforesaid facilities, and the several costs of those acquired during 1917 as depreciated to January 1, 1918, and the several costs, without adjustment for depreciation of those acquired subsequent to December 31, 1917, with the
72 exception hereinafter mentioned, is shown in the second and third columns of schedule marked "Exhibit I" attached to defendant's Exhibit F, the first column showing the 1917 and 1918 costs, less depreciation for 1917, and the second column the 1919 costs. Said schedules show the costs of such facilities, with the exception that the sum of $340,000, expended in the purchase of a limestone dock is to be added to the first item in the second column, opposite the words "Raw Material Equipment." Said defendant's Exhibit F has been received in evidence, and said second and third columns of Exhibit I attached thereto are now referred thereto and made part hereof as though fully set forth.

13. At the time of filing its said return for 1918, the plaintiff duly made claim for deduction from gross income under section 234 (a) (8) of the revenue act of 1918 on account of amortization of the said facilities, which claim was subsequently revised by the plaintiff and the revised claim for $1,756,453.64 filed with the commissioner on or about September 10, 1921.

14. Sometime in September, 1921, the commissioner, acting by the authorized officials of the amortization section of the Income Tax Unit of the Bureau of Internal Revenue, sent his representative, one W. F. R. Griffith, an engineer in said amortization section, to the plaintiff's properties with written instructions and authority to examine the same, investigate the facts and matters set out in the plaintiff's said revised claim, audit said claim in the light of
73 such investigation, and submit to said amortization section a report of the plaintiff's amortization allowance and a determination of said allowance and the amount thereof.

15. Said Griffith carried out his said instructions and on or about October 23, 1921, made a detailed, written report to said amortization section covering his said examination and investigation and audit and his findings of fact in the course thereof and containing his recommendation and determination that the plaintiff be allowed an amortization allowance of $1,344,465.15 of which $1,245,448.21 should be deducted from 1918 gross income and $99,016.94 from 1919 gross income.

16. In the ordinary and usual course of business of the Income Tax Unit, and said amortization section thereof, said report and determination of Griffith came on for review before one B. L. Wheeler, chief of engineers in said amortization section and duly authorized by the commissioner in that behalf, and upon such review and consideration thereof the said B. L. Wheeler approved said report and determination in all respects, and on or about December 1, 1921, signified his approval in writing endorsed on said report.

17. On or about the 1st day of December, 1921, and in the ordinary and usual course of business of the Income Tax Unit and said amortization section, said report and determination came for
74 action before one T. J. S. Kishpaugh, acting chief of said amortization section, who then and there approved said report and signified his approval by endorsement in writing thereon.

18. On or about the 2nd day of December, 1921, a copy of said report, with said endorsements thereon, was delivered to the plaintiff by said amortization section on behalf of and with the authority of the commissioner.

19. The commissioner did not at any time after December 1, 1921, and before March 3, 1924, make any reexamination or reinvestigation or further examination or investigation of the matter of the plaintiff's amortization allowance or obtain any further facts or evidence with respect to the same, or take any further action whatsoever in that behalf, or determine that or consider whether said allowance of $1,344,465.15 was otherwise than correct.

20. The plaintiff did not at any time subsequent to said determination of December 1, 1921, make any protest against the amount or legality thereof or request any reexamination of its return in regard thereto, or request any examination or further examination or reexamination, or any investigation or reinvestigation or further investigation of the matter of its amortization allowance. On the contrary, the plaintiff accepted said determination as correct and proper and took no further action whatsoever with respect thereto.

75 21. Subsequent to March 3, 1924, to wit, on or about October 1, 1924, some person in said amortization section (then called appraisal section), unknown to the plaintiff, assigned the matter of said allowance to one L. E. Luce, an appraisal engineer in said amortization section (then called appraisal section), to be reinvestigated and reexamined, but neither the said Luce nor any

other person took any action in that behalf, nor was any further action taken in the Income Tax Unit with respect to the plaintiff's amortization allowance until on or about April 1, 1925.

22. On or about April 1, 1925, the said Luce went to Painesville, Ohio, for the purpose of examining the plant of the plaintiff. He arrived at or about 10.00 a. m. and left at or about 4.00 p. m. on the same day.

23. On or about November 4, 1925, Luce made a report to the amortization section (then called appraisal section), stating in such report that $468,812.30 was the amortization deduction to which the plaintiff was entitled.

24. The said last-mentioned report was entitled on the covering page thereof "Report on Redetermination of Amortization Claim of the Diamond Alkali Company, Pittsburgh, Pennsylvania." In the text of said document the report and determination of said W. F. R. Griffith was referred to as a "first determination" and the report of said Luce as a "first redetermination." Said report of Luce contained the further statement in the last paragraph
76 thereof that "the allowances herein recommended are in lieu of those previously made." Said report of Luce was approved, by signed writing thereon, by Felder Furlow, reviewing engineer, and J. T. Keenan, then chief of said appraisal section (formerly amortization section).

25. On or about November 4, 1925, said appraisal section (formerly amortization section) sent to the plaintiff a copy of said so-called "Report on Redetermination of Amortization Claim of the Diamond Alkali Company, Pittsburgh, Pennsylvania."

26. On or about November 17, 1926, the plaintiff received from said appraisal section (formerly amortization section) a paper entitled on the covering page thereof "Office Report on Second Redetermination of the Amortization Claim of the Diamond Alkali Company, Pittsburgh, Pennsylvania," wherein the plaintiff's amortization allowance was stated to be $387,224.40, of which $369,022.30 was apportioned to 1918 and $18,202.10 to 1919. Said so-called second redetermination was made by said L. E. Luce in the first instance, without, however, any further examination of the plaintiff's properties, and was approved, by signed endorsement thereon, by M. W. Nolan, reviewing engineer in said appraisal section (formerly amortization section) and J. M. Clack, then chief of said section. In said "office report on second redetermination" said document of November 4, 1925, was referred to as "report on the
77 first redetermination" and the said so-called "office report on second redetermination" contained in the last paragraph thereof the statement that "the allowances herein recommended are in lieu of those previously made."

27. Said so-called "office report on second redetermination" was used by the commissioner in his last computation of the plaintiff's

net income for 1918 and in assessing the alleged additional tax for that year which is sought to be recovered in this action.

28. The allowances specified in said two reports of Luce were not based on the discovery of any fraud in connection with said first determination stated in said Griffith report, or on any new and material evidence not available to W. F. R. Griffith, or on any mathematical error or mistake in the said report.

29. At all times involved in this proceeding the plaintiff was engaged in the manufacture of alkali by the Solvey process. The alkali manufactured by it during 1918 consisted of soda-ash or sodium carbonate and caustic soda. During that year it began the installation of facilities to manufacture sodium bicarbonate, another alkali. The manufacture of these alkali products involved a commercial application of a chemical process and required the employment of many facilities of various kinds. These facilities were connected, intermingled, interdependent, and interrelated.

30. The said determination made on or about December 1,
78 1921, was predicated on the plaintiff's manufacturing plant being one harmonious unit or whole made up of mutually interdependent facilities, but said redeterminations or attempted redeterminations based on said reports of L. E. Luce were based on the theory that the plaintiff's plant was composed of sections or parts severable from the unit or whole and not of mutually interdependent and nonseverable facilities.

31. The soda-ash capacity of the plaintiff's plant was fixed by the capacity of the furnaces employed in the final step of producing soda-ash.

32. At the end of the amortization period, that is after the addition of war-time facilities, and during the post-war period, there were forty-one soda-ash furnaces in plaintiff's plant. Under normal conditions not over four furnaces would be kept idle continuously for the purposes of making necessary repairs and adjustments; and not less than thirty-seven could be kept in continuous operation, twenty-four hours per day, three hundred and sixty-five days per year.

33. The capacity of each furnace at the end of the amortization period and during the post-war period, under normal conditions, was forty tons of soda-ash per day, or 33,250 tons per month.

34. The actual average per month production of the plaintiff's plant for the post-war period, to wit, March 3, 1921, to March 3, 1924, was 22,597 tons of soda-ash.

79 35. The plant of the plaintiff as enlarged by the war-time facilities was in excess of the needs of the plaintiff during the post-war period.

36. The "value in use," that is, the ratio of the actual use of the facilities to the use of which they were capable, during the post-war period is represented by the fraction $\frac{22597}{33250}$ or 32%; and the percentage which represents the extent to which the facilities were not necessary for the postwar use is 68%.

37. A reasonable deduction on account of amortization of plaintiff's war-time facilities is $120,793.24, being an amortization of $27,755.21 upon such facilities acquired in 1919 at a cost of $86,735.02, and an allocation to 1919 taxes of $93,038.03 of a total amortization of $646,996.01 upon facilities acquired in 1917 and 1918, said sum of $93,038.03 being 14.38% of said total amortization of facilities acquired prior to January 1, 1919. Said allocation of 14.38% of the amortization upon war-time facilities acquired in 1917 and 1918 was "spread" to 1919 taxes by reason of the fact that such facilities were used as war-time facilities until March 31, 1919, and the plaintiff's income from January 1, 1919, to March 31, 1919, was 14.38% of its total income during the entire war period, that is, from January 1, 1919, to March 31, 1919.

38. Exhibit 1, attached hereto, is a correct computation of the plaintiff's income and profits taxes for the year 1919.

80 39. Plaintiff is entitled to judgment for the full amount of its claim, $7,340.26, and interest from December 15, 1920.

EXHIBIT 1

SCHEDULE

1919 taxes

Net income		$2,708,248.07
Less additional amortization		49,525.73
		$2,658,722.34
Excess-profits tax at 18.31% of net income as determined by commissioner		$486,812.06
Income tax:		
Income		$2,658,722.34
Less:		
Liberty bond interest	$69,981.11	
Excess-profits tax	486,812.06	
Specific exemption	2,000.00	
		558,793.17
Taxable at 10%		$2,099,929.17
	or	$209,992.92
Tax liability:		
Excess-profits tax		$486,812.06
Taxable at 10%		209,992.92
Total tax liability		$696,804.98
Tax paid with return		711,379.02
81 Correct tax liability		696,804.98
Tax overpaid		$14,574.04
Overpayment credited		1,467.64
		$13,106.40

CONCLUSIONS OF LAW

The plaintiff has brought suit to recover an alleged overpayment of 1919 taxes, with interest. The claim is based upon an alleged

insufficient deduction for amortization upon plaintiff's war-time facilities obtained in the year 1919.

The instant case was tried at the same time as a case between the plaintiff and D. B. Heiner, collector of internal revenue, at No. 5762 law, wherein the plaintiff's 1918 taxes were in issue. The amortization deductions for the years 1918 and 1919 are closely related, and we have discussed the reasons leading to our decision in this case in our opinion in the case at No. 5762 law. For reasons therein set forth, we have determined that the correct amortization deduction from plaintiff's income, upon 1919 costs, was $27,755.21, and not $18,202.10, as held by the commissioner; and we have found that the amount of the deduction from 1919 income due to allocation of amortization allowance upon 1918 costs to 1919 income was $93,038.01, instead of $53,065.41, as found by the commissioner. The plaintiff, by these determinations, was entitled to an additional deduc-
82 tion of $49,525.73 from 1919. This deduction allowed, the amount of plaintiff's taxes for 1919 is found to be $14,574.04 less than the amount actually paid. The commissioner has already credited plaintiff with $1,467.64, as the amount of overpayment admitted by him. This sum deducted, the existing overpayment is $13,106.40.

As the overpayment is in excess of the amount claimed in plaintiff's statement, plaintiff is entitled to a judgment for the full amount claimed, $7,340.26, with interest from December 15, 1920.

In United States District Court for the Western District of Pennsylvania

No. 5761 law

DIAMOND ALKALI COMPANY, A CORPORATION

vs.

C. G. LEWELLYN, FORMERLY COLLECTOR OF INTERNAL REVENUE FOR the 23rd District of Pennsylvania

Order for Judgment

And now, to wit, February 10, 1930, it is hereby ordered that judgment be entered for the plaintiff, Diamond Alkali Company, and against the defendant, C. G. Lewellyn, former collector of
83 internal revenue, in the amount of eleven thousand, three hundred seventy-one and 32/100 ($11,371.32) dollars.

Per Curiam.

G.

And now, to wit, April 19, 1930, exception noted on behalf of the defendant to such of his requests for specific findings of fact as have not been included by the court in his findings of fact, and bill sealed.

R. M. GIBSON, [SEAL.]
District Judge.

In United States District Court

Motion to vacate judgment

And now, to wit, February 14th, 1930, comes Diamond Alkali ompany, plaintiff above named, by its attorneys, Smith, Shaw, cClay & Seifert, and moves this honorable court to vacate the dgment entered in the above entitled case on February 10, 1930, r the following reasons:

1. Section 177 (b) of the judicial code as amended by section 615 the revenue act of 1928, provides:

"(b) In any judgment of any court rendered (whether against e United States, a collector or deputy collector of internal revenue, a former collector or deputy collector, or the personal representative in case of death) for any overpayment in respect of any internal-revenue tax, interest shall be allowed at the te of 6 per centum per annum upon the amount of the overpayent, from the date of the payment or collection thereof to a date eceding the date of the refund check by not more than thirty days, ch date to be determined by the Commissioner of Internal evenue."

the judgment entered herein, interest has been calculated on the incipal sum to which the plaintiff is entitled under the opinion om the date of payment to the date of judgment.

The general counsel of the Bureau of Internal Revenue and the omptroller General of the United States have requested that all ch judgments be entered for the principal amount of tax and terest paid by plaintiff and which it is entitled to recover " with terest from the date of payment as provided by law." This cilitates the calculation of interest by the disbursing clerk of the easury Department.

2. The court has found as a fact that Exhibit 1 attached to its inion is a correct computation of the plaintiff's income and profits xes for the year 1919; that exhibit shows that the plaintiff has overid its tax in the amount of $13,106.40; that finding is to be conlered as the equivalent of a verdict of a jury.

In Pennsylvania a plaintiff is entitled after verdict in excess the amount claimed to amend the statement of claim, in order that the averments therein may agree with the verdict.

Wherefore, plaintiff prays this honorable court to vacate the judgment aforesaid, and (a) permit plaintiff to amend its tement of claim to agree with the findings of fact, a copy of which nendment is being presented with this motion; and (b) enter judgent in favor of the plaintiff, Diamond Alkali Company, and ainst the defendant, C. G. Lewellyn, in the sum of $13,106.40 with terest thereon from December 15, 1920.

SMITH, SHAW, MCCLAY & SEIFERT,
Attorneys for Plaintiff.

Order

And now, to wit, February 14th, 1930, the foregoing motion having been presented in open court, upon consideration thereof and upon motion of W. W. Booth of counsel for plaintiff, it is hereby ordered that the judgment entered herein on February 10, 1930, be and the same is hereby vacated; that plaintiff's amendment to its statement of claim be and the same is hereby accepted, and ordered filed; and it is further ordered that judgment be entered in favor of the plaintiff, Diamond Alkali Company, and against the defendant, C. G. Lewellyn, formerly collector of internal revenue, in the sum of $13,106.40, with interest thereon from December 15, 1920, as provided by law.

Exception reserved to defendant and bill sealed.

Per curiam.

G.

86 In United States District Court

Judgment

February 14, 1930, pursuant to above order judgment is hereby entered in favor of the plaintiff, Diamond Alkali Company, and against the defendant, C. G. Lewellyn, former collector of internal revenue, in the sum of $13,106.40, with interest thereon from Dec. 15, 1929.

J. Wood Clark,
Clerk.

In United States District Court

Petition for appeal

Filed May 13, 1930

The defendant, C. G. Lewellyn, formerly collector of internal revenue for the twenty-third district of Pennsylvania, by his attorneys, conceiving himself aggrieved by the judgment made and entered on the 14th day of February, A. D. 1930, in the above-entitled case, does hereby appeal from said judgment to the United States Circuit Court of Appeals for the Third Circuit, for the reasons specified in the assignments of error, which are filed herewith, and he prays that this appeal may be allowed and that a transcript of the record, proceedings and papers upon which said judgment was made and entered, duly authenticated, may be sent to the United States Circuit Court of Appeals for the Third Circuit.

Louis E. Graham,
United States Attorney for the Western District of Pennsylvania.
John A. McCann,
Special Assistant to the U. S. Attorney,
Attorneys for the Defendant.

87 *Order*

The foregoing petition for appeal is allowed this 13th day of May, A. D. 1930.

R. M. Gibson.

In United States District Court

Assignments of error

Filed May 13, 1930

Comes now the defendant, C. G. Lewellyn, formerly collector of internal revenue for the twenty-third district of Pennsylvania, by his attorneys, and in connection with his petition for appeal in the above entitled case, files the following assignments of error:

1. The court erred in rendering judgment for the plaintiff.

2. The court erred in failing to render judgment in favor of the defendant.

3. The court erred in applying the rate of 19.8% in determining plaintiff's war profits and excess profits tax for the year 1919.

4. The court erred in applying to the determination of plaintiff's war profits and excess profits taxes for the year 1919 the "special assessment" rate used by the Commissioner of Internal Revenue in granting the plaintiff relief under the provisions of sections 327 and 328 of the revenue act of 1918.

88 5. The court erred in failing to calculate plaintiff's war profits and excess profits taxes for the year 1919 for the purpose of this case, under the provisions of section 301 of the revenue act of 1918.

6. The court erred in increasing plaintiff's invested capital for the year 1919 by the amount determined by the court to have been overpaid by plaintiff as Federal taxes for prior years.

89-106 [Omitted.]

107 70. The court erred in concluding as a matter of law that:

108 "For reasons therein set forth, we have determined that the correct amortization deduction from plaintiff's income, upon 1919 costs, was $27.755.21, and not $18,202.10, as held by the commissioner; and we have found that the amount of the deduction from 1919 income due to allocation of amortization allowance upon 1918 costs to 1919 income was $93,038.01, instead of $53,085.41, as found by the commissioner. The plaintiff, by these determinations, was entitled to an additional deduction of $49,525.73 from 1919. This deduction allowed, the amount of plaintiff's taxes for 1919 is found to be $14,574.04 less than the amount actually paid. The commissioner has already credited plaintiff with $1,467.64, as the amount of overpayment admitted by him. This sum deducted, the existing overpayment is $13,106.40."

71. The court erred in concluding as a matter of law that:

"As the overpayment is in excess of the amount claimed in plaintiff's statement, plaintiff is entitled to a judgment for the full amount claimed, $7,340.26, with interest from December 15, 1920."

72. The court erred in failing to conclude, as a matter of law, that plaintiff had not overpaid its tax in any amount whatsoever for the year 1919.

73. The court erred in failing to conclude, as a matter of law, that judgment should be for the defendant.

109 Wherefore defendant prays that the judgment rendered herein be reversed, with directions to the District Court of the United States for the Western District of Pennsylvania to enter judgment in favor of the defendant below.

LOUIS E. GRAHAM,
United States Attorney for the Western District of Pennsylvania,
JOHN A. MCCANN,
Special Assistant to the U. S. Attorney,
Attorneys for the Defendant.

MAY 13, A. D. 1930.

In United States District Court

Certificate of probable cause

And now, on this 23rd day of April, A. D. 1930, the court, having been fully advised in the premises, hereby certifies that, inasmuch as the collector of internal revenue was acting pursuant to instructions from the Commissioner of Internal Revenue, there was probable cause for the collection of Federal taxes and interest thereon from the plaintiff, as shown by the record in this cause.

Per curiam.

G.

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110 In United States District Court

Stipulation for printing the record

It is hereby stipulated and agreed by and between the parties hereto, by their respective counsel, that the following be printed as and constitute the record on the pending appeal of the defendant to the United States Circuit Court of Appeals for the Third Circuit in the above-entitled case:

1. Docket entries.
2. All pleadings.
3. Bill of exceptions and stipulation with reference thereto.
4. Judgment.
5. Petition for appeal and order allowing appeal.
6. Assignments of error.
7. This stipulation.
8. Clerk's certificate.

SMITH, SHAW, MCCLAY & SEIFERT.
Attorneys for the Plaintiff.
LOUIS E. GRAHAM,
United States Attorney.
W. J. AIKEN,
Asst. U. S. Attorney.
Attorneys for the Defendant.

111 [Clerk's certificate to foregoing transcript omitted in printing.]

United States Circuit Court of Appeals for the Third Circuit

No. 4427 (List No. 50). October term, 19—

C. G. LEWELLYN, FORMERLY COLLECTOR, APPELLANT

vs.

DIAMOND ALKALI CO., APPELLEE

On appeal from the District Court of the United States for the Western District of Pennsylvania

And now, to wit, this 15th day of January, A. D. 1930, it is ordered that Hon. J. Whitaker Thompson, district judge for the Eastern District of Pennsylvania, and Hon. , district judge for the District of , be, and he hereby, assigned to sit in above case in order to make a full court.

JOSEPH BUFFINGTON, *Circuit Judge.*

[Endorsements:] 4427. Order assigning Hon. J. Whitaker Thompson for argument. Recd. & filed Jan. 15, 1931. Wm. P. Rowland, clerk.

In the United States Circuit Court of Appeals for the Third Circuit

No. 4427. October term, 1930

C. G. LEWELLYN, FORMERLY COLLECTOR, APPELLANT

vs.

DIAMOND ALKALI CO., APPELLEE

And afterwards, to wit, the 15th day of January, 1931, come the parties aforesaid by their counsel aforesaid, and this case being called for argument sur pleadings and briefs, before the honorable Joseph Buffington and honorable J. Warren Davis, circuit judges, and honorable J. Whitaker Thompson, district judge, and the court not being fully advised in the premises, takes further time for the consideration thereof.

And afterwards, to wit, on the 10th day of February, 1932, come the parties aforesaid by their counsel aforesaid, and the court, now being fully advised in the premises, renders the following decision:

In the United States Circuit Court of Appeals for the Third Circuit

No. 4419. October term, 1930

DIAMOND ALKALI COMPANY, APPELLANT

v.

D. B. HEINER, COLLECTOR, APPELLEE

No. 4426. October term, 1930

D. B. HEINER, COLLECTOR, APPELLANT

v.

DIAMOND ALKALI COMPANY, APPELLEE

No. 4427. October term, 1930

C. G. LEWELLYN, FORMERLY COLLECTOR, APPELLANT

v.

DIAMOND ALKALI COMPANY, APPELLEE

Upon appeals from the United States District Court for the Western District of Pennsylvania

Opinion

Filed February 10, 1932

Before BUFFINGTON and DAVIS, Circuit Judges, and THOMPSON, District Judge

THOMPSON, Circuit Judge (sworn in as circuit judge February 3, 1931):

These cases were tried by the court below under a stipulation of the parties without a jury. Diamond Alkali Company, the taxpayer plaintiff below, was engaged in the manufacture of soda ash and related products. It filed its income and profits tax returns for the years 1918 and 1920 on June 16, 1919, and May 13, 1921, respectively, and paid the amounts shown therein as due. Thereafter the Commissioner of Internal Revenue assessed as additional taxes and interest the sum of $1,398,548.54 and collected the same on November 15, 1927, more than five years after the returns.

The plaintiff's claim for refund was rejected by the commissioner and suit was thereupon instituted in the District Court for the Western District of Pennsylvania as of No. 5762. Judgment was entered for the plaintiff in the sum of $175,410.60. The case is before this court on cross appeals Nos. 4419 and 4426.

Suit was also brought by the Diamond Alkali Company as of No. 5761 for the recovery of alleged overpayment of taxes for the year

1919. Judgment was entered for the plaintiff in that suit for $13,106.40. Appeal No. 4427 is taken by the collector of internal revenue alone from that judgment.

Appeals Nos. 4419 and 4426

The plaintiff's claims for refunds for the years 1918 and 1920 were based on the following general contentions: That the Commissioner of Internal Revenue unlawfully assessed additional taxes for the years 1918 and 1920 after the statute of limitations had run; that the 1918 allowance for amortization of war-time facilities was inadequate; that the allowance for depreciation for 1918 and 1920 was inadequate; that the invested capital for 1920 was wrongfully reduced by the unlawful collection of additional taxes for 1917; that the commissioner assessed excess-profits taxes for 1918 at a rate higher than that lawfully applicable.

The District Court held that the additional assessment for 1918 and 1920 was not barred by the statute; that the amount allowed for amortization by the commissioner was inadequate in several respects; that the amount allowed for depreciation was lawfully ascertained; that the plaintiff was entitled to have its 1920 invested capital increased by sums collected as additional taxes and interest for 1917; and that the court had no power to revise the rate fixed by the commissioner under the special-assessment provisions. In addition, it directed that the amount allowed for amortization be allocated to the years 1918 and 1919.

Statute of limitations

The plaintiff contended that it was entitled to a refund of all additional taxes assessed and collected after the statute of limitations had run, and based its contention upon section 250 (d) (1) of the revenue act of 1921, which reads as follows:

"The amount of income, excess-profits, or war-profits taxes due under any return made under this act for the taxable year 1921 or succeeding taxable years shall be determined and assessed by the commissioner within four years after the return was filed, and the amount of any such taxes due under any return made under this act for prior taxable years or under prior income, excess-profits, or war-profits tax acts, or under section 38 of the act entitled 'An act to provide revenue, equalize duties, and encourage the industries of the United States, and for other purposes,' approved August 5, 1909, shall be determined and assessed within five years after the return was filed, unless both the commissioner and the taxpayer consent in writing to a later determination, assessment, and collection of the tax; and no suit or proceeding for the collection of any such taxes due under this act or under prior income, excess-profits, or war-profits tax acts, or of any taxes due under section 38 of such act of August 5, 1909, shall be begun, after the expiration of five years after the date when such return was filed, but this shall not

affect suits or proceedings begun at the time of the passage of this act: * * *."

Prior to the expiration of the five-year period, the commissioner transmitted to the plaintiff an unexecuted agreement, by the terms of which for the assessment and collection of the 1918 taxes was extended beyond the statutory period. The agreement was signed by the plaintiff and returned to the commissioner, who acknowledged its receipt and stated that it was on file in his office. From time to time similar written agreements were transmitted by the commissioner to the plaintiff, signed by the plaintiff, and returned to the commissioner, extending the time for assessment and collection to December 31, 1927. Although no one of the agreements was signed by the Commissioner of Internal Revenue in person, all of them were signed in his name, were on file in his office, and were relied upon by him in acting upon the plaintiff's protests. The letters to the plaintiff with reference to the extension agreements went out in the regular course of business and were signed in the name of the assistant to the commissioner.

The cited statute requires only that the commissioner and the taxpayer consent in writing to the later determination, assessment, and collection. It does not require that the consent, in order to be valid, be in one instrument or in any particular form. In the instant case, the consent by the commissioner is found in the letters which were sent out from his office. Contentions against the validity of agreements of extension, because of the lack of the commissioner's signature, were unsuccessfully made in this court in Liberty Baking Company v. Heiner (37 F. (2d) 703). (See also Trustees for Ohio and Big Sandy Coal Company v. Commissioner, 43 F. (2d) 782 (C. C. A. 4); Sabin v. United States, 44 F. (2d) 70 (Ct. Cls.); Stern Bros. & Co. v. Burnet, 51 F. (2d) 1042 (C. C. A. 8).) In Stange v. United States (282 U. S. 270, 276) the court said:

"As pointed out in Florsheim Bros., etc., v. United States (280 U. S. 453, 466) a waiver is not a contract, and the provision requiring the commissioner's signature was inserted for purely administrative purposes and not to convert into a contract what is essentially a voluntary, unilateral waiver of a defense by the taxpayer."

We find no error in the conclusion of the District Court that the additional assessments for 1918 and 1920 were made within the proper statutory period as extended by the waivers.

Amortization

One of the conditions upon which the plaintiff relies in support of its claim for refund is based upon the commissioner's treatment of its claims under section 234 (a) (8) of the revenue act of 1918. In order to reimburse those who had incurred capital expenditures in their business for war purposes, that act provides:

"In the case of buildings, machinery, equipment, or other facilities constructed, erected, installed, or acquired, on or after April 6, 1917,

for the production of articles contributing to the prosecution of the present war, * * * there shall be allowed a reasonable deduction for the amortization of such part of the cost of such facilities * * * as has been borne by the taxpayer, but not again including any amount otherwise allowed under this title or previous acts of Congress as a deduction in computing net income. * * *."

The plaintiff constructed, erected, installed, and acquired after April 6, 1917, certain buildings, machinery, equipment, and other facilities for the production of articles contributing to the prosecution of the war against the German Government. With its income-tax return for 1918, it filed a claim for a deduction from gross income on account of the amortization of the cost of such facilities.

One Griffith, an engineer of the amortization section of the Bureau of Internal Revenue, made an investigation of the facts set out in plaintiff's amortization claim and about October 23, 1921, submitted a report in which he recommended an amortization allowance in the amount of $1,344,465.15. The report was approved by the chief of the amortization section. On December 2, 1921, in response to a request by the plaintiff, a copy of the report was sent to it accompanied by a letter which read as follows:

"Further reference is made to your letter of November 7, 1921, and reply from this office under date of November 9, 1921, making request for copy of report by the appraisal engineer who made investigation of the facilities involved in claim for amortization.

"Copy of the approved report submitted by the appraisal engineer is enclosed for your information.

"In transmitting a copy of this report, at the present time, upon request of the taxpayer, it is to be clearly understood that the merits of the case, and the correctness of the conclusions reached by the engineer, are not now to be made the subject of objection or conference, and that no further consideration can be given to the amortization claim until such time as the taxpayer is officially notified of the result of the complete audit and examination. Subsequent to transmittal of the usual formal letter, there is provided a thirty-day period wherein any objections by the taxpayer may be properly presented for the consideration of this office. The amortization feature of the case may be taken up only at that time, together with any other matters which the taxpayer may then desire to present."

Subsequent to March 3, 1924, the matter was assigned for reinvestigation to one Luce, another appraisal engineer in the amortization section. His final recommendation, made November 17, 1926, modifying a prior report of November 4, 1925, was that the plaintiff be allowed an amortization deduction of $387,224.40. The Commissioner of Internal Revenue based his determination of the amortization allowance on the Luce report.

It is contended by the plaintiff that the amortization allowance had been determined following the Griffith report and that any redetermination after March 2, 1924, was in violation of section 234 (a) (8) of the revenue act of 1921, which reads:

" * * * At any time before March 3, 1924, the commissioner may, and at the request of the taxpayer shall, re-examine the return, and if he then finds as a result of an appraisal or from other evidence that the deduction originally allowed was incorrect, the income, war-profits, and excess-profits taxes for the year or years affected shall be redetermined; * * *."

But that contention leaves out of consideration the effect of section 278 (b) of the revenue act of 1924, which reads:

"Any deficiency attributable to a change in a deduction tentatively allowed under * * * paragraph (8) of subdivision (a) of section 234, of the revenue act of 1918 or the revenue act of 1921, may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time."

We find no error in the finding and conclusion of the trial judge that the letter of December 2, 1921, fixed the deduction, reported by Griffith prior to March 3, 1924, as tentative and not final; nor in his conclusion of law that the power of determination had not yet passed from the commissioner, and did not pass from him prior to his issue of the thirty-day letter.

The final allowance followed the Luce report in November, 1926. Section 234 (a) (8) of the act of 1921 applies only in those cases in which the commissioner, having once determined and finally and not tentatively allowed the amortization deduction, then redetermines it. Under such circumstances the dead line is March 3, 1924. Under authority of section 278 (b), above cited, the commissioner had power to determine the deduction tentatively allowed at any time, and to collect in accordance with such determination.

In the cases of Commissioner v. Ohio Falls D. & F. Works (50 F. (2d) 660) and Norton Co. v. Commissioner (50 F. (2d) 664) the Sixth and First Circuits decided on the facts before them that the right granted to the commissioner by section 278 (b) to assess or collect deficiencies at any time was unavailable, since in each of those cases there had actually been more than a "tentative" allowance of the amortization deduction prior to March 3, 1924. In the instant case, the correspondence in the record and the finding of the trial judge convince us that any so-called allowance made immediately following the Griffith report and prior to March 3, 1924, was "tentative" within the meaning of section 278 (b).

In the court below, as previously indicated, the plaintiff contended that the method of computing the amortization allowance followed by the commissioner was erroneous; and that the commissioner improperly rejected claims for amortization upon the cost of a limestone dock and upon the cost of real estate purchased by the plaintiff during the war. Those subjects are discussed in the order named.

The plaintiff's plant had been enlarged by war-time facilities which were in excess of the needs of the plant during the postwar period, and it was therefore entitled to a deduction for amortization. The postwar period comprises the period between March 3, 1921, the date of the President's proclamation, and March 3, 1924 (U. S. Comp.

Stat. sec. 3115 14/15 f). During that time the plaintiff's plant produced an average of 22,597 tons of soda ash per month, and for the year showing peak production an average of 26,163 tons per month.

In order to ascertain the amount of the amortization allowance, the commissioner proceeded to determine the "value in use" or the "residual value," as it is commonly termed, of the war-time facilities. For that purpose he used the ratio which the postwar production bore to the war-time capacity, taking as the numerator of the fraction representing the ratio, the postwar production and as the denominator of the fraction the war-time plant capacity. The plaintiff had presented its claim to the commissioner on the broad principles of this formula. The figures which it used were:

22,597 tons per month (average postwar production per month).
45,017 " " " (war-time capacity).

The commissioner substituted the following figures:

26,163 tons per month (average per month of the postwar year showing peak production).
33,250 " " " (war-time capacity).

The District Court found from the evidence, as a fact, that the average war-time capacity of the plaintiff's plant was 33,250 tons per month and not 45,017 tons as claimed by the plaintiff. The commissioner and the court took the average war-time monthly production of 33,250 tons as plant capacity. That method might be justified if supported by the evidence. The witnesses, however, including the plaintiff's president, two industrial superintendents, and the former chief of the amortization section of the Bureau of Internal Revenue, unequivocally testified that the average monthly capacity of the plaintiff's plant was 45,017 and gave their reasons and the facts upon which they based their conclusion. The only testimony to the contrary was that of Luce. His testimony was based entirely on production records under war-time conditions. This was not a fair criterion by which to determine plant capacity. The court might have disbelieved the plaintiff's witnesses, but he did not base his conclusions upon that ground. It is apparent that he ignored the testimony of skilled and experienced witnesses, based upon actual facts, and reached a conclusion contrary to their testimony without any substantial evidence to sustain his conclusion. The question before him was not the average plant production during the war but the plant capacity. The learned judge must be held in error in his adoption of the figure of 33,250 tons as plant capacity, instead of 45,017 tons.

The trial judge, in finding the numerator of the fraction representing the ratio which postwar production bore to war-time capacity, rejected the commissioner's selection of the postwar year showing the peak production and adopted the contention of the plaintiff that the numerator should represent the average production of the plant per month during the whole postwar period and, therefore, found the value in use to be $\frac{22,597}{33,250}$ or 67+%.

Section 234 (a) (8) of the revenue act of 1918 provides that there shall be allowed "a reasonable deduction" for amortization. The regulations and the practice adopted by the commissioner provide for arriving at a deduction through means of a ratio showing the relation of war-time capacity to postwar production. To be "reasonable," the allowance must be, as the term implies, just, fair, and equitable. The regulations of the commissioner provide for using a ratio as a means of comparison and that method would be just, fair, and equitable, if properly applied. But the term "ratio" in itself means the relation which one quantity has to another of the same kind. In attempting to fix a ratio, the commissioner adopted a standard by which one term of the ratio (the numerator) is represented by the average production during one year only of the postwar period, that of peak production, and the other term (the denominator) by the monthly average production of the whole war-time period. The defendant contended vigorously for the figures representing the average monthly production during the war-time period and prevailed in having his theory adopted and in obtaining a finding by the trial judge of the figures representing that standard. In attempting to arrive at the term of the ratio representing the postwar period, however, he urged the adoption of the average production during the peak year of that period and not during the whole period. We can not agree that a just and fair relation between the two periods can be obtained by the inconsistent method proposed to be applied by the commissioner and urged on his behalf by the defendant. In our view, in order to obtain a reasonable allowance which is just, fair, and equitable, the quotient should be that of the ratio of similar terms.

The commissioner considered specific facilities or groups of facilities in computing the allowance. The plaintiff claimed that its plant was one harmonious unit and that the extent of the use of the various facilities comprising the plant could not be determined separately or by departments but only as a unit. All the pertinent facts were before the learned district judge in his capacity as a fact-finding tribunal. Under R. S. sec. 649 (28 U. S. C. A., sec. 773) the findings of fact by a judge, in the event that a jury has been waived, have the same effect as the verdict of a jury. The findings will not be disturbed where there is any evidence to sustain them. (Tarn v. United States, 16 F. (2d) 272 (C. C. A. 3); Ward v. Joslin, 186 U. S. 142.) In the latter case it was said:

"When a case is tried by the court without a jury, its findings on questions of fact are conclusive, although open to the contention that there was no evidence on which they could be based."

It nowhere appears that it was impossible to fix a value on the individual facilities and no sound reason is advanced by the plaintiff to induce the court to reverse the commissioner's action. No facts appear to support the plaintiff's contention that the absolute unity of the plant for amortization purposes is established. Section 234 (a) (8) of the revenue act of 1918 bases amortization upon "facil-

ities" and not upon the aggregate of the facilities united in one plant. In United States v. Briggs Mfg. Co. (40 F. (2d) 425, (C. C. A. 2)) specific facilities were considered by the commissioner in determining the amortization allowance. In Appeal of Manville Jenckes Co. (4 B. T. A. 765) it is said:

"The deduction contemplated by the statute is 'a reasonable deduction for the amortization of such part of the cost of such (amortizable) facilities or vessels as has been borne by the taxpayer.' The deduction is in respect of specific facilities."

We find no error in the classification of facilities by the District Court.

The plaintiff purchased a limestone dock in 1917 at a cost of $340,000. The District Court permitted 32 per cent amortization on the total cost of the dock. The commissioner had disallowed any amortization. The defendant contends that the dock was purchased from an affiliated company, the Fairport, Painesville & Eastern R. R. Company, and that amortization does not apply to property transferred from one affiliated company to another. The record does not contain any proof convincing to the trial court that the plaintiff corporation was affiliated with that company in 1917, the year in which the dock was purchased. There is sufficient testimony to warrant the trial court's finding of fact that the limestone dock was in excess of the plaintiff's peace-time requirements. We therefore find no error in the allowance of 32 per cent on the cost of the dock. In view of our approval of the allowance by the District Court of amortization on the cost of the dock, it is directed that the depreciation allowed by the commissioner on the same cost be deducted from the determined amortized allowance.

The plaintiff claimed full amortization on the cost of land purchased by it at the total cost of $96,989.60 in 1917 and $108,979.50 in 1918. The purchase was made in order to settle actions for damages brought against the plaintiff by the owners of the land. It was conceded that no part of the plaintiff's plant was erected upon the land and that it was wholly useless to the plaintiff both during and after the war. The commissioner refused to make any allowance on the ground that land is not subject to amortization. The statute permits an amortization allowance on "buildings, machinery, equipment, or other facilities." Amortization is therefore limited to the facilities named or those ejusdem generis. (United States v. Baumgartner, 259 Fed. 722.) Finally the land was not used for the production contemplated by Congress. The case of United States v. Corono Coal Co. (23 F. (2d) 673), cited by the plaintiff, is readily distinguished from the case at bar. In that case amortization was allowed on the cost of a shaft driven through earth and rock to get at coal. A mining shaft is obviously a facility necessary to mining operations. The land for which amortization was claimed does not come within the class meant by Congress by the phrase "other facilities."

The District Court allocated the allowance for amortization over the years 1918 and 1919 in accordance with the percentages previously determined by the commissioner. Article 185 of Regulations 62 of the Treasury Department provides that an amortization allowance shall be apportioned in cases where the property was employed in the production of articles contributing to the prosecution of the war over the respective accounting periods of the taxpayer, having reasonable regard to the gross income and net income. The defendant contends that, since the court altered the income from that established by the commissioner through an additional amortization allowance, it should alter the percentage of such an allowance deductible in each year. The regulations, however, provide that:

"The amortization allowance shall be spread in proportion to the net income (computed without benefit of the amortization allowance) * * *."

It is therefore obvious that the percentages for the years 1918 and 1919, as determined by the commissioner, are unaffected by the increased amortization allowance.

Depreciation

The commissioner allowed a composite depreciation rate of 10.4 per cent for all of the plaintiff's depreciable assets for the years 1917 and 1920, inclusive. This amounted to $437,262.55 for 1918 less than half the $876,366.71 claimed by the plaintiff. The District Court sustained the action of the commissioner.

The plaintiff does not complain of the depreciation rate which was applied for 1917, 1919, and 1920, but insists that the rate for the year 1918 should be 20 per cent or more. The basis for this contention is that, during that year, poor labor conditions resulting in direct damage to and neglect of the machinery, inadequate repairs due to the lack of mechanics, and poor fuel caused a rapid deterioration of the plant. Whether the amount the commissioner caused to be deducted for depreciation under those circumstances was right, is a question of fact. The burden of proving the contrary is on the taxpayer. We said in Rieck v. Heiner (25 F. (2d) 453; certiorari denied, 277 U. S. 608):

"Nor is there a burden on the commissioner, when he has formally determined an amount of depreciation, to prove it right as a condition to sustaining the assessment by showing the investigation he has pursued and the matters that have influenced his judgment in arriving at it, for having found the depreciation and having made an assessment based on it, the law presumes his action right and the assessment prima facie valid."

The plaintiff did assume the burden of proving that the depreciation rate allowed by the commissioner for 1918 was wrong, but, in the judgment of the trial judge, failed. We see no error in his conclusion.

The revnue acts of 1918 and 1921, sections 234 (a) (7), provide that, in computing the net income of a corporation subject to tax, "a reasonable allowance for the exhaustion, wear and tear of prop-

erty used in the trade or business, including a reasonable allowance for obsolescence" shall be made. While a "reasonable" allowance is not defined in the statutes, we have hereinabove defined it as one that is just, fair, and equitable.

Although the deduction allowable on account of depreciation is to be based upon the actual wear and tear sustained during that year, it is obvious that actual wear and tear of machinery and equipment is not ordinarily susceptible of scientific measurement in any one year. The commissioner determined that the average life of the equipment in the plaintiff's plant was from nine to ten years, and therefore determined the composite depreciation allowance of 10.4 per cent. The plaintiff can not take credit for an accelerated depreciation rate for the one year of 1918 without subjecting its taxes for 1917, 1919, and 1920 to revision by the commissioner. The commissioner's determination of the rate of depreciation will not be disturbed in the absence of fact findings sufficient to convince us of error in law by the court below.

The plaintiff contends that it was entitled to a deduction for depreciation at the proper rate upon the unamortized cost of its war facilities. The defendant maintains that, in computing the residual value of the property, the depreciation factor had already been considered. The District Court did not pass upon this contention in its findings of fact or conclusions of law. In the absence of any reference in the briefs of either party to facts upon the record sustaining their respective contentions, we do not deem this question properly presented for decision.

Invested capital for 1920

The District Court filed its opinion February 10, 1930. At that time there was a judgment in favor of the plaintiff for an alleged overpayment of taxes for 1916 and 1917 in the case of Diamond Alkali Company v. Heiner (39 F. (2d) 643). The basis for that judgment was that these taxes had been collected after the expiration of the appropriate statutory limitation period. Subsequent to the filing of the opinion of the District Court in the case at bar, an appeal, taken by the defendant to this court from the judgment rendered in that case, was decided in favor of the defendant. (See Heiner v. Diamond Alkali Company, 49 F. (2d) 120.) That decision is sustained by that of the Supreme Court in Graham and Foster v. Goodcell (282 U. S. 409). Since the judgment in favor of the plaintiff for the alleged overpayment of taxes for 1916 and 1917 has been reversed by this court, the plaintiff is not entitled to have the sum of $269,451.93 credited to its 1920 capital, as directed by the court below. The District Court was therefore in error in holding that the capital of the plaintiff for 1920 should be thus increased.

Special assessment

Upon application of the plaintiff, the commissioner found that its excess-profits tax for 1918, as determined without the benefit of section

327 of the revenue act of 1918, would, owing to abnormal conditions affecting its capital or income, work upon it an exceptional hardship evidenced by gross disproportion between the tax computed without the benefit of the said section and the tax computed by reference to the representative corporations specified in section 328. The commissioner determined the amount due as plaintiff's excess-profits tax for 1918 as $2,084,324.26 on the basis of a net income of $3,821,143.63. The ratio of tax to net income therefore, as determined by the commissioner, was 54.54 per cent. The plaintiff's contention in the District Court was that the rate of 54.54 per cent was not justified by the evidence and that the rate should be 45 per cent. The District Court having reduced the net income for 1918 and applied the rate determined by the commissioner, to wit, 54.54 per cent, to the reduced income, the contention was abandoned. The defendant's position, on appeal, is that, the District Court being without jurisdiction to review the action of the commissoner in determining whether a special assessment should be made under sections 327 and 328 of the revenue act of 1918 (Williamsport Wire Rope Company v. United States, 277 U. S. 551; see also Cramer & King Co. v. Commissioner, 41 F. (2d) 24), it follows that the commissioner's action in determining the amount of the plaintiff's excess-profits tax under sections 327 and 328 is not subject to judicial review.

In Brown's "Shamrock" Linens, Ltd., v. Bowers (41 F. (2d) 862) the commissioner had allowed a special assessment and computed the excess-profits tax in accordance with section 328 of the revenue act of 1918 at the rate of 44.8 per cent of its net income. The taxpayer complained that the rate was excessive and should have been 25 per cent. The court there held that section 328 vested in the commissioner administrative discretion in the computation of the tax and that his discretion was not subject to judicial review. This ruling was affirmed by the Circuit Court for the Second Circuit in 48 F. (2d) 103. The question appears to have been settled by the Supreme Court in favor of the commissioner's contention when it refused a certiorari in Brown's "Shamrock" Linens, Ltd., v. Bowers, Executor (283 U. S. 865).

The District Court was therefore in error in redetermining the amount of the excess-profits tax fixed by the commissioner.

Appeal No. 4427

We have disposed of the questions involved in this appeal in the opinion upon Appeals Nos. 4419 and 4426.

The cases will be remanded to the District Court for modification of its judgments in accordance with the foregoing opinion.

A true copy. Teste:

_____,

Clerk of the United States Circuit Court of Appeals for the Third Circuit.

In the United States Circuit Court of Appeals for the Third Circuit

No. 4427 (List No. 50). October term, 1930

C. G. LEWELLYN, FORMER COLLECTOR, APPELLANT

vs.

DIAMOND ALKALI COMPANY, APPELLEE

On appeal from the District Court of the United States for the Western District of Pennsylvania

This cause came on to be heard on the transcript of record from the District Court of the United States for the Western District of Pennsylvania and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this court that the judgment of the said District Court in this cause be, and the same is hereby, modified, with direction to the said District Court to enter a new judgment in accordance with the opinion of this court.

Philadelphia, February 10, 1932.

J. W. THOMPSON, *Circuit Judge.*

[Endorsements:] 4427. Order modifying judgment, etc. Recd. & filed Feb. 10, 1932. Wm. P. Rowland, clerk.

United States Circuit Court of Appeals for the Third Circuit

October term, 1930

No. 4419

DIAMOND ALKALI COMPANY, APPELLANT

against

D. B. HEINER, COLLECTOR, APPELLEE

No. 4426

D. B. HEINER, COLLECTOR, APPELLANT

against

DIAMOND ALKALI COMPANY, APPELLEE

No. 4427

C. G. LEWELLYN, FORMERLY COLLECTOR, APPELLANT

against

DIAMOND ALKALI COMPANY, APPELLEE

Upon appeals from the United States District Court for the Western District of Pennsylvania

John W. Davis, William A. Seifert, Maynard Teall, Marion N. Fisher, counsel for the appellant, Diamond Alkali Company.

[Endorsed:] Recd. & filed Mar. 5, 1932. William P. Rowland, clerk.

Petition of appellant for rehearing

To the Honorable the Justices of the Said Court:

I

These cases arise on appeals from two judgments of the District Court of the United States for the Western District of Pennsylvania. They involve the income and excess-profits tax liability of Diamond Alkali Company for the years 1918, 1919, and 1920. Nos. 4419 and 4426 are cross appeals from one of the judgments of the court below rendered with respect to the years 1918 and 1920. No. 4427 is an appeal by the defendant below from the judgment of the lower court for the year 1919. This petition is specifically addressed to Nos. 4419 and 4426 in so far as they relate to the income and profits tax liability of Diamond Alkali Company for the year 1918 and to No. 4427 in so far as it relates to the profits-tax liability for 1919. Since the decision of this court was so recently rendered, a complete restatement of the facts and the questions of law involved would not seem necessary, and this petition is confined to the particular facts and questions of law relied upon in support of this request for rehearing.

II

The decision announced by the court in its opinion filed February 10, 1932, holds that although the net income of $3,821,134.63 found by the Commissioner of Internal Revenue should be reduced to $3,385,540.81 (a reduction of $435,593.82) the profits tax of $2,084,324.26 found by the commissioner may not be correspondingly reduced. In mathematical result this is equivalent to holding that the profits tax rate of 54.54% found by the commissioner by means of special assessment should be increased to 61.59%. We believe that this court can scarcely have realized the anomaly of this outcome and the extraordinary results that follow from the principle employed. We believe and respectfully submit that the court has not construed sections 327 and 328 of the 1918 revenue act in accordance with the intent of Congress and prior decisions by the courts.

The effect of the decision

There was imposed, and the appellant paid, a profits tax amounting to 54.54% of the net income which the commissioner determined, as well as an income tax of 12% based on the same net income. The court has found that the net income was incorrectly computed by the commissioner since the amortization deduction allowed by the commissioner was inadequate. It has allowed an additional deduction of $435,593.02 for the year 1918 on account of amortization of war facilities, thus reducing the taxable net income by $435,593.02. The

income tax assessed upon this sum at 12% is some $52,270, which the court holds to be an overpayment. Applying to the same figure the profits-tax rate of 54.54% would indicate a similar overpayment on that account of some $237,572. Nevertheless the court by its decision holds the first to be recoverable but refuses to allow the second. It seems to us that the two must inevitably rise or fall together. In each case the tax must be predicated upon the taxpayer's true net income.

We do not believe that the special-assessment provisions (relief provisions) of the 1918 act, or the decisions of the courts, wherein they have construed this statute, require this result. If the principle adopted by this court is sound, it may be applied generally. Let us suppose that this taxpayer had prevailed in its suit throughout and had obtained as it claimed an additional amortization deduction for 1918 amounting to $929,491.32 and an additional depreciation deduction of $439,104.16. Its net income then would have been $2,352,548.15. The profits tax which this court has said may not be disturbed amounts to considerably more than 80% of this net income. In other words, the principle employed by the court would be tantamount to increasing the ratio of profits tax to true net income from 54.54% to more than 80%. It could hardly be said that relief results from the so-called relief provisions if they are to be so applied. On the actual facts of this case the court under the theory of not disturbing the commissioner's determination of special assessment has in effect increased the ratio of profits tax to net income from 54.54% to 61.59% of the correct net income. Has not the court redetermined the profits-tax rate by special assessment?

If the principle is sound it should be susceptible of a further test. Suppose this taxpayer had by its suit shown errors in the net income as determined by the commissioner with the result that its correct net income was found to be only $2,000,000. Under the principle employed the fixed amount of profits tax then would be found to be more than 100% of the correct net income. And it would follow that if any taxpayer whose profits tax had been determined under special assessment should bring suit and should prove that by reason of losses not allowed by the commissioner it in fact had no net income, it would still be left under a large profits tax, although it had no net income, and this notwithstanding the fact that the statute imposes the profits tax upon net income alone.

These are logical results which might easily flow from an application of the principle adopted by the court.

Sections 327 and 328 provide a means for determining the rate of tax as distinguished from the tax itself

Like other taxes on net income the profits tax is the result of multiplying a net income by a rate. The special assessment provisions are not used to determine the net income. The average net income of other comparative corporations is not used as a substitute

for the taxpayer's net income; it is the taxpayer's own net income that is used. Nor do those provisions directly fix the tax. They specifically and solely provide a means of determining the ratio of net income that shall be taken as a tax; that is, they relate solely to a special means for arriving at a rate of profits tax. This rate, once determined by special assessment must be applied to the correct net income.

We believe that the court has been led by false reasoning of the appellee to the conclusion that special assessment is the means of procuring the tax itself, instead of the rate which must then be applied to a net income before a tax is found. The error is fundamental and far-reaching.

The only case cited by the court and the case which it deemed to be controlling is Brown's Shamrock Linens, Ltd. v. Bowers (48 Fed. (2nd) 103). In that case the taxpayer admitted the correctness of the net income which the commissioner found and complained only of the rate. The taxpayer did not go before the court saying that an erroneous tax had been determined by special assessment, but that an erroneous rate of taxation had been determined by that means. The court so viewed the issue, saying:

"Thus it is apparent that the complaint attacks the correctness of the ratio used by the commissioner and asks the court to review all the comparative data which under the statute must enter into his determination of such ratio."

The court then went on to say that on the authority of Williamsport wire Rope Co. v. United States (277 U. S. 551) the majority of the court were of the opinion that the taxpayer's contention that the court review the comparatives must be denied.

In the case at bar the appellant abandoned its claim that the rate of 54.54% found by the commissioner was too high because improper comparatives had been used (the statement of claim having been filed before the Supreme Court's decision in the Williamsport Wire Rope case). The Government contended that the court was without jurisdiction to review the case at all and in reply the appellant contended that since the rate of 54.54% was not reviewable it should be applied to whatever net income the court might finally determine to be correct. But neither party presented argument leading to the result reached by the court.

We repeat that the factor which is here determined by the commissioner from the use of comparatives is the profits-tax rate and not the profits tax itself. The determination of the tax once the rate has been determined is merely a matter of mathematical computation. The process of performing this simple mathematical function is surely not one of discretion.

If net income is reduced, the profits-tax rate may not be increased

In the course of the oral argument of this case, the Government handed up a typewritten reply brief, which was later printed and

filed, in which it contended that the court should not take jurisdiction of the case, because if the commissioner should determine the profits-tax rate by special assessment on a reduced net income he might find a rate higher than 54.54%. This argument is wholly fallacious, and appellant has not heretofore had an opportunity to answer it specifically.

The profits tax provided by the statute is a graduated tax; that is, a part of the net income of 1918 is taxed at 30%, a certain excess is taxed at 65%, and a further excess, if any, is taxed at 80%. (1918 act, section 301). Obviously if the net income is reduced to any extent, that part falling in the 80% bracket will be lessened or eliminated, and if the reduction be sufficient that part falling in the 65% bracket will be lessened or eliminated. Therefore the inevitable effect under the statute of a reduction in net income is a reduction in the ratio of the total profits tax to the total net income.

A profits-tax rate determined from comparatives (by special assessment) must be derived from comparatives whose profits taxes have been determined in the regular manner, that is, at graduated rates (section 328). The statute provides for the selection of comparatives that are similarly circumstanced as to capital, net income, etc. The only change which this court was asked to make in 1918 or did make for 1918 was a reduction in net income. The abnormality on which the commissioner held that the taxpayer was entitled to special assessment was one of capital and not of income. (See offer of proof, B. E., p. 222.) If the commission had reduced this taxpayer's net income by $435,000 and had turned to other comparatives, it would not have been proper to employ comparatives whose invested capital was greatly less than those already used. Such new comparatives, if indeed new comparatives would seem necessary for a relatively small change in net income, would be comparatives with the same or approximately the same invested capital but with reduced net income. Necessarily the profits-tax rate so obtained could not exceed the 54.54% originally fixed and probably would substantially less.

The Government's argument in the reply brief mentioned above is based on grossly distorted and improper illustrations of how a recomputation of the tax, after reduction of net income, might be made by special assessment. In each illustration, particularly in Nos. 1 and 2 (pp. 15, 16), forced results are obtained by methods that would undoubtedly amount to serious abuse of discretion if employed in actual practice. Plaintiff confidently asserts that the impropriety of the methods employed by way of illustration can be demonstrated if opportunity is afforded to it to file a brief and reargue the question.

The view taken by this court on the special assessment issue was not suggested by either party to the litigation. It goes far beyond the requirements of the statute and the decision in Williamsport

Wire Rope Company v. United States (277 U. S. 551). It means that, if in any case special assessment be allowed, then, for the purposes of excess-profits taxes, determinations of taxable income by the commissioner, however erroneous, arbitrary, or invalid they may be, are not subject to any review or correction whatsoever. No argument has been offered directly upon the position taken by the court either in the briefs or at the bar. This question is so substantial both as to matter of law and the amount of tax involved that, we submit, briefs and oral argument upon it should be presented.

The foregoing applies likewise to the year 1919, No. 4427.

III

Another question is whether the taxpayer is entitled to depreciation for 1918 on the unamortized cost of depreciable assets; that is, whether the taxpayer is entitled to a deduction for depreciation on such part of the assets as remain after deducting the allowance for amortization. This question is decided by the court adversely to the taxpayer. Indeed the court not only declined to increase the commissioner's allowance, but the court also disallowed a part of the depreciation allowed by the commissioner, namely, the depreciation on the limestone dock, which cost $340,000. Since the composite rate of depreciation was 10.4%, the court has reduced the depreciation allowance made by the commissioner by the sum of $35,360.

On the matter of deduction in 1918 for obsolescence of war facilities (obsolescence being one of the factors of so-called depreciation), the Supreme Court of the United States decided in favor of the taxpayer in the case of United States Cartridge Company v. United States. This decision was handed down by the Supreme Court on February 15, 1932, and is reported in the United States Daily of February 19, 1932. In that case the Supreme Court's construction of the statute relating to depreciation and amortization, subsections (7) and (8), section 234, revenue act of 1918) fully supports the appellant's contention and is contrary to the principle upon which this court necessarily proceeded in excluding depreciation on the entire cost of the limestone dock.

The court suggested in its opinion that the briefs did not point to facts in the record upon which a depreciation allowance could be made upon unamortized costs of war facilities. Since plaintiff was contending that amortization should be allowed on more facilities than the court below recognized, it was not feasible to burden otherwise lengthy briefs with various tabulations of specific facilities and their costs less amortization deductions. Appellant's briefs were prepared on the basis that once the court decided which facilities should be subject to amortization it would be a simple matter to compute unamortized costs of such facilities as the additional depreciation base. If the appellant is given opportunity to do so, it can

readily set forth from the exhibits introduced the specific facilities and their unamortized costs which should be the basis for additional depreciation.

Wherefore, the appellant prays that this court will grant a rehearing in these causes.

JOHN W. DAVIS,
WILLIAM A. SEIFERT,
MAYNARD TEALL,
MARION N. FISHER,
Counsel for the Appellant, Diamond Alkali Company.

We, John W. Davis, William A. Seifert, Maynard Teall, and Marion N. Fisher, of counsel for the appellant, Diamond Alkali Company, do hereby certify that the foregoing petition for a rehearing of these causes is presented in good faith and not for delay.

JOHN W. DAVIS.
MARION N. FISHER.
WILLIAM A. SEIFERT.
MAYNARD TEALL.

In the United States Circuit Court of Appeals for the Third Circuit

No. 4427. October term, 1930

C. G. LEWELLYN, FORMER COLLECTOR, APPELLANT

vs.

DIAMOND ALKALI CO., APPELLEE

Sur petition for rehearing

And now, to wit, April 5, 1932, after due consideration, the petition for rehearing in the above-entitled case is hereby granted.

Philadelphia.

J. W. THOMPSON, *Circuit Judge.*

[Endorsements:] 4427. Order granting petition for rehearing. Recd. & filed Apr. 5, 1932. Wm. P. Rowland, clerk.

In the United States Circuit Court of Appeals for the Third Circuit

No. 4427. October term, 1930

C. G. LEWELLYN, FORMERLY COLLECTOR, APPELLANT

vs.

DIAMOND ALKALI CO., APPELLEE

And afterwards, to wit, the 15th day of April, 1932, come the parties aforesaid by their counsel aforesaid, and this case being called for reargument sur pleadings and briefs, before the honorable Joseph Buffington, honorable J. Warren Davis, and honorable J. Whitaker

Thompson, circuit judges, and the court not being fully advised in the premises, takes further time for the consideration thereof.

And afterwards, to wit, on the 26th day of July, 1932, come the parties aforesaid by their counsel aforesaid, and the court, now being fully advised in the premises, renders the following decision:

In the United States Circuit Court of Appeals for the Third Circuit

No. 4419. March term, 1932

DIAMOND ALKALI COMPANY, A CORPORATION, PLAINTIFF-APPELLANT

v.

D. B. HEINER, COLLECTOR OF INTERNAL REVENUE FOR THE TWENTY-third District of Pennsylvania, defendant-appellee

No. 4426. March term, 1932

D. B. HEINER, COLLECTOR, APPELLANT

v.

DIAMOND ALKALI COMPANY, APPELLEE

No. 4427. March term, 1932

C. G. LEWELLYN, FORMERLY COLLECTOR, APPELLANT

v.

DIAMOND ALKALI COMPANY, APPELLEE

Upon appeals from the District Court of the United States for the Western District of Pennsylvania

Opinion

Filed July 26, 1932

Before BUFFINGTON, DAVIS, and THOMPSON, Circuit Judges

DAVIS, Circuit Judge:

The Diamond Alkali Company filed a petition for rehearing on two points and seeks:

1. To have the tax rate of 54.54 per cent and 18.31 per cent, determined by the commissioner in a special assessment, to be the fair and just rate for this corporation for 1918 and 1919, respectively, applied to its income as reduced by the decision of this court.

2. A deduction for depreciation on so much of its war facilities as were not amortized.

These questions will be considered in the above order.

1. The taxes for 1918 and 1919 are involved. The commissioner allowed a deduction for 1918 for amortization of war facilities of

$315,956.89 and for 1919 a deduction of $71,267.51. But this court on reversing the redetermination of the Board of Tax Appeals allowed a deduction for 1918 of $790,187.16 and a deduction for 1919 of $175,838.94, making a total allowance for both years of $966,026.10 instead of $327,224.40 allowed by the commissioner. The net income of the petitioner, as determined by the commissioner for 1918, was $3,921,143.63 and for 1919, $2,708,248.07. Applying the rate of 54.54 per cent to the income of 1918 as determined by him, the commissioner found that the company owed a profits tax of $2,084,-324.26 for that year, and applying the rate of 18.31 per cent to the income for 1919, he found it owed a profits tax of $495,871.87 for that year.

The net income of the petitioner for the two years was reduced by our former decision by $578,801.70, yet the commissioner insists, and we held, that the total amount of the tax should not be reduced. If it is not reduced, it would result in a tax rate of 61.62 per cent for 1918 and a rate of 19.05 per cent for 1919 instead of 54.54 per cent and 18.31 per cent for those years, respectively, as fixed by the commissioner. This new rate would in effect be fixed by the court, which allowed deductions, but refused to apply the rate fixed by the commissioner to the reduced income. In other words, if the contention of the collector prevails, the petitioner will pay the same tax for the two years that it would have paid if its taxable income had not been reduced by $578,801.70. The collector contends that although the corporation's income was reduced more than one-half million dollars, its tax must nevertheless remain the same for the reason that this court is without power to review the commissioner's determination of the taxpayer's liability for taxes, inasmuch as the taxes were determined by a special assessment.

The allowance or denial of a special assessment provided for in sections 327 and 328 of the revenue act of 1918 is an administrative question committed to the discretion or judgment of the Commissioner of Internal Revenue, subject, however, to review by the Board of Tax Appeals. Whether or not there are abnormal conditions affecting capital, as alleged in this case, or income which would work upon the corporations an exceptional hardship without the benefit of a special assessment; what are representative corporations to be used as comparatives, engaged in a like or similar trade or business; whether or not they are similarly circumstanced with respect to income, profits per unit of business transacted and capital employed, the amount and rate of war profits or excess profits, and all other relevant facts and circumstances, are questions for the sole determination of the commissioner. (Blair v. Oesterlein Machine Company, 275 U. S. 220; Williamsport Wire and Rope Company v. United States, 277 U. S. 551, 559.) They have been committed by Congress to his judgment and discretion, which may not be exercised by the court. He has considered all these questions and in the light of all the facts has determined rates which must be accepted by the court as fixed, fair, and just. In holding that the rates fixed by him

shall be applied to the petitioner's true income the court does not usurp the discretionary functions expressly conferred upon him.

The collector raises the objection that if the commissioner had not made a mistake in not allowing proper depreciation, other representative corporations might have been selected from which a different rate might have been fixed. This may or may not be true. It is purely suppositious. But when the commissioner applied these rates found and fixed by him as the proper ones to an improper income, and thus unjustly increased the taxes of the petitioner, the court does have power to order that the proper rate be applied to the proper income so that the taxpayer will pay only a proper and just tax. The power of the commissioner to determine an abnormality, to select representative corporations as comparatives, to allow a special assessment and fix the rate thereof, does not carry with it power so to fix the income on which the profits tax must be computed that an admittedly unjust amount of the tax is put beyond the review of the court. It is a bare possibility that the reduction of the income to the proper and just amount might have some conceivable effect on the selection of representative corporations. That was a matter for the commissioner, but when he found the correct rate he could not apply it to an incorrect and false income and produce an unjust tax.

2. The second question is whether or not the taxpayer should have been allowed depreciation on so much of the war facilities as were not amortized.

The taxpayer's contention is tersely presented in the following statement:

1. Facilities based on production of soda ash:	
1917 cost less depreciation	$543,082.60
Amortization allowed, 49.803% of cost	270,473.60
Unamortized cost	$272,609.00
1918 cost	$1,062,144.35
Amortization allowed, 49.8034% of cost	499,101.96
Unamortized cost	$563,042.39
2. Boiler-house equipment:	
1917 cost	$56,583.88
Amortization, 15%	8,487.58
Unamortized cost	$48,096.30
1918 cost	$140,015.57
Amortization, 15%	21,002.34
Unamortized cost	$129,013.23
3. Flaking machine:	
1918 cost	$2,880.00
Amortization allowed	1,631.81
Unamortized cost	$1,248.19

4. Six tank cars:		
1918 cost		$23,655.00
Amortization allowed		13,402.92
Unamortized cost		$10,252.08
1917 unamortized costs on which depreciation at 10.4% is claimed:		
(1)	$272,609.00	
(2)	48,096.30	
	$320,705.30	
10.4% of above is	$33,353.35	
1918 unamortized costs on which depreciation at 5.2% is claimed:		
(1)	$503,042.39	
(2)	129,013.23	
(3)	1,248.19	
(4)	10,252.08	
	$643,555.89	
5.2% of above is	$33,464.91	

The commissioner did not allow any amortization on the limestone dock, which cost $340,000, but the District Court did allow amortization at the rate of 32 per cent, or a deduction of $108,800. This much of the cost of the limestone dock which has been allowed by way of amortization should not be included in the depreciation base for the commissioner had already allowed depreciation at the rate of 10.4 per cent on the entire cost of $340,000. Therefore, 10.4 per cent of the amortized cost should be deducted from any additional depreciation. This is 10.4 per cent of $108,800, or $11,315.20.

The total additional depreciation claimed by the taxpayer is therefore as follows:

10.4% of unamortized 1917 costs		$33,353.35
5.2% of unamortized 1918 costs		33,464.91
		66,818.26
Less 10.4% of $108,800, amortized cost of dock		11,315.20
Additional depreciation		55,503.06

There is no contention, if we correctly understand the parties, that the above statement is not correct as to amounts and rate of depreciation, if depreciation is to be allowed in addition to allowance for amortization.

There is a question, however, as to whether or not amortization was intended to exclude depreciation for obsolescence or wear and tear. This is shown by the legislative history of the sections in question of the revenue act of 1918 (40 Stat. 1077), which controls this case. The Committee on Ways and Means, having charge of this measure, in its report, said that many facilities provided for war purposes would be of little value after the end of the war; that under the law then existing it was impossible to allow deductions other than for "ordinary exhaustion, wear and tear, and depletion of such property" and that the purpose of the provision was "to allow special amounts for amortization, according to the peculiar conditions in

each case." (House Report 767, 65th Congress, 2d session, p. 10; Senate Report 617, 65th Congress, 3d session, p. 7.) It is thus evidence that the allowance for amortization was not intended to exclude allowance for depreciation on unamortized war facilities. This question is settled by the case of the United States Cartridge Company v. United States (284 U. S. 511, 516), where the Supreme Court in construing this provision said that "deductions for amortization were not intended to exclude obsolescence, but rather were to be made in addition or having regard to allowances deducted on account of obsolescence and the like."

The record, it seems to us, shows that the allowances made were for amortization only and not for depreciation for exhaustion, wear, tear, and obsolescence for the year 1918. The taxpayer is entitled to a deduction for depreciation for exhaustion, wear, tear, and obsolescence on its unamortized war facilities. No question has been raised as to the correctness of the composite rate of 10.4 per cent for depreciation for exhaustion, etc., on war facilities installed in 1917 and 5.2 per cent on those installed in 1918.

The order of the court is that the rates fixed by the commissioner for the years 1918 and 1919 will be applied to the reduced income and that the order of the District Court denying deductions for depreciation on unamortized war facilities is reversed.

Thompson, Circuit Judge, dissents.

A true copy. Teste:

_____,

Clerk of the United States Circuit Court of Appeals for the Third Circuit.

In the United States Circuit Court of Appeals for the Third Circuit

No. 4427 (List No. 50). October term 1930

C. G. Lewellyn, Formerly Collector, appellant

vs.

Diamond Alkali Company, appellee

On appeal from the District Court of the United States for the Western District of Pennsylvania

This cause came on to be heard on the transcript of record from the District Court of the United States for the Western District of Pennsylvania and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this court that the judgment of the said District Court in this cause be, and the same is hereby, modified, with direction to the said District Court to enter a new judgment in accordance with the opinion of this court, as further modified by the opinion of this court

upon reargument, in that the said District Court is directed to apply the rates fixed by the commissioner for 1919 to the reduced income as indicated by the two opinions of this court.

Philadelphia, July 26, 1932.

J. WARREN DAVIS, *Circuit Judge.*

[Endorsements:] 4427. Order modifying judgment, etc. Recd. & filed July 26, 1932. Wm. P. Rowland, clerk.

UNITED STATES OF AMERICA.

Eastern District of Pennsylvania, Third Judicial Circuit, Set.:

I, William P. Rowland, clerk of the United States Circuit Court of Appeals for the Third Circuit, do hereby certify the foregoing to be a true and faithful copy of the original transcript of record and proceedings in this court in the case of C. G. Lewellyn, formerly collector, appellant, vs. Diamond Alkali Company, appellee, No. 4427, on file and now remaining among the records of the said court in my office.

In testimony whereof, I have hereunto subscribed my name and affixed the seal of the said court, at Philadelphia, this 19th day of October, in the year of our Lord one thousand nine hundred and thirty-two and of the independence of the United States the one hundred and fifty-seventh.

[SEAL.] WM. P. ROWLAND,
Clerk of the U. S. Circuit Court of Appeals, Third Circuit.

U. S. GOVERNMENT PRINTING OFFICE: 1932

137 Supreme Court of the United States

No. 478—October Term, 1932

Order allowing certiorari

Filed December 5, 1932

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

○

CLERK'S COPY.

TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1932

No. 478

C. G. LEWELLYN, FORMERLY COLLECTOR OF INTERNAL REVENUE FOR THE TWENTY-THIRD DISTRICT OF PENNSYLVANIA, PETITIONER

vs.

DIAMOND ALKALI COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

PETITION FOR CERTIORARI FILED OCTOBER 26, 1932

CERTIORARI GRANTED DECEMBER 5, 1932

(37175)

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1932

No. 478

C. G. LEWELLYN, FORMERLY COLLECTOR OF INTERNAL REVENUE FOR THE TWENTY-THIRD DISTRICT OF PENNSYLVANIA, PETITIONER

vs.

DIAMOND ALKALI COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

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1 In United States District Court, Western District of Pennsylvania

Docket entries

Aug. 25, 1928, præcipe for for summons filed. Statement of claim filed. Summons issued.

Aug. 27, 1928, summons returned served on C. G. Lewellyn at Pittsburgh, on Aug. 27, 1928.

Sept. 10, 1928, affidavit of service of statement filed.

Sept. 21, 1928, præcipe for appearance of John D. Meyer and John A. McCann for defendant filed.

Nov. 9, 1928, affidavit of defense filed.

Jan. 14, 1929, plaintiff's reply to the new matter alleged in defendant's affidavit of defense filed.

Jan. 15, 1929, hearing on preliminary matters.

Jan. 21, 1929, stipulation waiving jury trial filed. Trial opens, before Gibson J., without a jury.

Jan. 22, 1929, trial continues.

Jan. 23, 1929, trial continues. Motion for judgment for plaintiff filed. Motion for judgment for defendant filed.

Jan. 24, 1929, trial closed. Trial memo. filed.

Feb. 5, 1929, transcript of testimony filed.

2 Feb. 23, 1929, plaintiff's request for findings of fact filed at No. 5762 Law.

Feb. 10, 1930, opinion and order filed and entered directing that judgment be entered for the plaintiff and against the defendant in the sum of $11,371.32.

Pursuant to the above order, judgment is hereby entered for the plaintiff, Diamond Alkali Company, against the defendant, C. G. Lewellyn, former collector of internal revenue, in the sum of $11,371.32.

J. Wood Clark, *Clerk.*

Feb. 14, 1930, on motion of plaintiff, order entered vacating the above judgment entered on Feb. 10, 1930; allowing the plaintiff to file an amendment to its statement of claim; and directing that judgment be entered for the plaintiff and against the defendant in the sum of $13,106.40 with interest thereon from Dec. 15, 1920; exception reserved to defendant and bill sealed.

Feb. 14, 1930, amendment to statement of claim filed.

Feb. 14, 1930, pursuant to the above order, judgment is hereby entered in favor of the plaintiff, Diamond Alkali Company, and against the defendant, C. G. Lewellyn, former collector of internal revenue, in the sum of $13,106.40, with interest thereon from Dec. 15, 1920.

J. Wood Clark, *Clerk.*

Apr. 23, 1930, certificate of probable cause filed.

May 13, 1930, on petition of C. G. Lewellyn, order entered allowing appeal. Assignments of error filed. Order of court filed and entered permitting defendant until Wednesday, May 28, 1930, to file bills of exception. Citation issued.

May 27, 1930, stipulation for printing appeal record filed.

May 27, 1930, on stipulation, order entered allowing and settling certain matter in the bill of exceptions in the case at No. 5762 law, together with certain other matter in this case, as the bill of exceptions in this case.

In United States District Court

Statement of Claim

Filed Aug. 25, 1928

Diamond Alkali Company, the above-named plaintiff, has a claim against C. G. Lewellyn, formerly collector of internal revenue for the twenty-third district of Pennsylvania, defendant, for the sum of $7,340.26, with interest thereon from the 15th day of December, 1920, upon a cause of action whereof the following is a statement:

1. Diamond Alkali Company, the plaintiff, is, and at all
4 times herein mentioned was, a corporation organized and existing under the laws of the State of West Virginia, with its principal office in the city of Pittsburgh in the Commonwealth of Pennsylvania.

2. C. G. Lewellyn, the defendant, was, from the 1st day of October, 1914, until the 31st day of July, 1921, the duly appointed, qualified, and acting collector of internal revenue for the twenty-third district of Pennsylvania and now resides in the city of Pittsburgh and within said western district.

3. For the year 1919 the plaintiff kept its books of account on the accrual basis and filed its Federal income and profits-tax return on the accrual and calendar year basis.

4. On the 12th day of May, 1920, the plaintiff duly filed its said return for 1919 and paid to the defendant as collector of internal revenue for the twenty-third district of Pennsylvania the income and profits taxes appearing by said return to be owing to the Government of the United States, to wit, $711,379.02.

5. Only $702,571.12 of said tax of $711,379.02 was in fact owing and $8,807.90 thereof was an overpayment. Said overpayment was made by plaintiff to defendant on or about December 15, 1920. $1,467.64 thereof has been allowed to plaintiff as a credit on alleged additional taxes for 1918, leaving a net overpayment of $7,340.26.

6. By letter dated July 11, 1927, the Commissioner of In-
5 ternal Revenue (hereinafter called the "commissioner") notified the plaintiff that its income and profits tax return for 1919 was erroneous; that he, the commissioner, had made divers

changes and adjustments in the plaintiff's tax liability and in the figures on which the same was computed; and that as the result of such changes and adjustments plaintiff had overpaid the sum of $1,467.64.

7. The change and adjustment which resulted in alleged overpayment of $1,467.64 instead of the correct amount of overpayment, $8,807.90, was as follows: Redetermination of the plaintiff's allowance for the amortization of war-time facilities under section 234 (a) (8) of the revenue act of 1918 in the sum of $387,224.40 instead of permitting the same to stand at $1,344,465.15 as determined at the time and in the manner hereinafter described, whereby the plaintiff's deduction from 1919 gross income on account of said allowance was changed from $99,016.94 to $18,202.10.

8. Said tax of $711,379.02 and the assessment and collection thereof were and are erroneous, illegal, and void to the extent of $8,807.90. Annexed hereto, marked Exhibit 1, and made part hereof is a correct statement of the plaintiff's income and profits tax liability for the year 1919, showing the amount actually owing, the amount the plaintiff was compelled to pay, and the amount of tax paid by plaintiff in excess of the amount owing and for the recovery of which this suit is brought.

9. At all times up to and including the third day of March,
6 1924, the amortization section of the Income Tax Unit and the employees thereof had full charge on the part of the commissioner of audit, investigation, and consideration of claims by taxpayers under section 234 (a) (8) of the revenue act of 1918 and section 234 (a) (8) of the revenue act of 1921 for allowances on account of amortization of war-time facilities, and at all such times the chief or acting chief of said section had full power and authority from the commissioner, as plaintiff avers on information and belief, to determine the amount of such allowances and give notice of such determinations to the claimants, and as a matter of regular routine and practice did make such determinations and give such notices with full knowledge, acquiescence, and approval on the part of the commissioner and without consideration or action by the commissioner personally.

10. Plaintiff constructed, erected, installed, and acquired on or after April 6, 1917, certain buildings, machinery, equipment, and other facilities for the production of articles contributing to the prosecution of the war with Germany, and at the time of filing its said return, plaintiff duly made claim for deduction from gross income under section 234 (a) (8) of the revenue act of 1918 on account of amortization of war-time facilities, which claim was subsequently revised by the plaintiff, and the revised claim for $1,756,453.64 filed with the commissioner on or about September 10, 1921. Said sum of $1,756,453.64 was and is the correct amortization allowance to which the plaintiff was as a matter of fact entitled, and $269,451.86 thereof was deductible from plaintiff's gross income for 1919.

7 11. In the month of September, 1921, the commissioner, acting by the authorized officials of said amortization section, sent his representative, one F. R. Griffith, an engineer in said amortization section, to the plaintiff's properties with written instructions and authority to examine the same, investigate the facts and matters set out in the plaintiff's said revised claim, audit said claim in the light of such investigation, and submit a report and determination of the plaintiff's allowance under section 234 (a) (8) of the revenue act of 1918 to said amortization section.

12. Said Griffith carried out his said instructions and on or about October 23, 1921, made a detailed written report to said amortization section covering his said examination, investigation, and audit and his findings of fact in the course thereof, and containing a determination that the plaintiff was entitled to an allowance under said section 234 (a) (8) in the sum, as plaintiff avers on information and belief, of $1,344,465.15, of which $1,245,448.21 should be deducted from 1918 gross income and $99,016.94 from 1919 gross income.

13. In the ordinary and usual course of business of the Income Tax Unit and said amortization section thereof, said report and determination came for review before one B. L. Wheeler, chief of engineers in said amortization section and duly authorized by the commissioner in that behalf, and upon such review and consideration thereof the said B. L. Wheeler approved said report and deter-

8 mination in all respects, and on or about December 1, 1921, signified his approval in writing endorsed on said report.

14. On or about the 1st day of December, 1921, and in the ordinary and usual course of business of the Income Tax Unit and said amortization section, said report and determination came for final action before one T. J. S. Kishpaugh, acting chief of said amortization section and, as plaintiff avers on information and belief, authorized by the commissioner to take such final action and to make determination of the plaintiff's allowance with the same effect as if by the commissioner personally, and said Kishpaugh then and there approved said report and determination and signified his approval by endorsement in writing on said report.

15. On or about the 10th day of January, 1922, a copy of said report and determination, with said endorsements thereon, was delivered to the plaintiff by said amortization section on behalf of and with the authority of the commissioner and, notwithstanding that the correct allowance was $1,756,453.64 as aforesaid, was nevertheless accepted by the plaintiff without further objection.

16. The plaintiff never thereafter requested a reexamination of its said returns with respect to said allowance. The commissioner did not thereafter at any time before March 3, 1924, reexamine said return with respect to said allowance, or determine that said

9 allowance of $1,344,465.15 was erroneous, or make or begin or cause to be made or begun any new investigation or reexamination of said allowance, or make any appraisal, or obtain any other evidence, or take any further action, or do any other thing whatso-

ever in respect to said allowance. On the contrary, plaintiff avers on information and belief that from the time of said approval of said determination of $1,344,465.15 by said acting chief of section as above described to on or about October 1, 1924, no further proceedings were had or taken with respect to plaintiff's amortization allowance, the same having been finally and definitely determined as hereinbefore averred.

17. On or about October 1, 1924, some person in said amortization section unknown to the plaintiff assigned the matter of said allowance for reexamination. No reexamination or reinvestigation was made or begun, however, until on or about April 1, 1925, when one Luce, an engineer in said amortization section, made an investigation and examination of plaintiff's properties; and on or about November 4, 1925, said Luce made a report to said amortization section covering his investigation and examination, and containing an alleged determination of plaintiff's said allowance at $468,812.30. On or about November 4, 1925, said amortization section sent to the plaintiff a copy of said report and determination entitled "Redetermination of Taxpayer's Claim for Amortization."

18. On or about November 17, 1926, the plaintiff received
10 from said amortization section a paper entitled "Second Redetermination of Amortization Claim," wherein the plaintiff's said allowance was alleged to be determined at $387,224.40, of which $369,022.30 was apportioned to 1918 and $18,202.10 to 1919.

19. Said alleged "Second Redetermination" was used by the commissioner in computing the plaintiff's net income and tax for 1919 as stated in his said letter of July 11, 1927.

20. Plaintiff is advised by counsel and therefore avers that it was and is lawfully entitled to said allowance in the sum of $1,344,465.15 regularly and finally determined as above described, and to deduction of $99,016.94 thereof from its 1919 gross income, and that said two subsequent alleged redeterminations under the circumstances above set forth, and being subsequent to March 3, 1924, were and are in violation of section 234 (a) (8) of the revenue act of 1921, and of no legal effect whatsoever, and plaintiff further avers that the said alleged redeterminations were not based upon any new and material evidence or any mathematical error or mistake or the discovery of any fraud in the original determination theretofore made.

21. On or about the 11th day of March, 1925, the plaintiff filed with the commissioner, on the form prescribed by him for that purpose, claim for refund of said overpayment of tax in the sum of $8,807.90 on the ground that said tax and the assessment and collection thereof were erroneous, illegal, and void to the extent of
11 said overpayment, but on or about July 11, 1927, the commissioner rejected said claim except $1,467.64 thereof.

22. Except for $1,467.64, no part of said overpayment of $8,807.90 has been repaid or refunded to the plaintiff.

Wherefore, this suit is brought and plaintiff claims judgment against the defendant for the sum of $7,340.26, with interest thereon from the 15th day of December, 1920.

SMITH, SHAW & MCCLAY,
Attorneys for Plaintiff.

Duly sworn to by W. E. Jones; jurat omitted in printing.

12 *Exhibit 1 to statement of claim*

1919

Net income			$2,680,498.64
Excess profits tax @ 18.31% of net income as determined by commissioner			490,799.30
Income tax:			
Income		$2,680,498.64	
Less exemptions—			
Liberty bond interest	$69,981.11		
Excess profits tax	490,799.30		
Specific exemptions	2,000.00		
		562,780.41	
Taxable @ 10%		2,117,718.23	211,771.82
Correct tax liability			$702,571.12
Paid with return			711,379.02
Overpayment			$8,807.90
Allowed by commissioner as credit against tax for 1918 on 11/15/27			1,467.64
Tax overpaid			$7,340.26

13 In United States District Court

Affidavit of defense

Filed Nov. 9, 1928

C. G. Lewellyn, defendant above named, alleges that he has a full, just, true, and legal defense to all of the plaintiff's statement of claim; and that the defense is of the following character:

1. Defendant admits the allegations contained in paragraph 1 of the statement of claim.

2. Defendant admits the allegations contained in paragraph 2 of the statement of claim.

3. Defendant admits the allegations contained in paragraph 3 of the statement of claim.

4. Defendant admits the allegations contained in paragraph 4 of the statement of claim.

5. In answer to the allegations contained in paragraph 5 of the statement of claim, defendant denies that only $702,571.12 of said tax of $711,379.02 was in fact owing and denies that $8,807.90 thereof was an overpayment. On the contrary, defendant alleges that $709,911.38 was in truth and in fact due and owing from plaintiff as

income and excess profits taxes for the year 1919; and that the correct amount of said overpayment for said year was in fact $1,467.64, the amount allowed to plaintiff, leaving no net overpayment. Defendant admits that said $8,807.90 (mentioned in
14 said paragraph 5 and herein above described), being part of said $711,379.02 above mentioned, was paid to the defendant on or about December 15, 1920.

6. The allegations of paragraph 6 of the statement of claim are admitted. But defendant alleges that the tax of the plaintiff for the years 1918, 1919, and 1920, respectively, was in process of audit by the Commissioner of Internal Revenue continuously from the respective dates of the filing of plaintiff's tax returns for said years to July 11, 1927. Said letter of July 11, 1927, stated only the final adjustments made in said tax liability of the plaintiff.

7. In answer to the allegations contained in paragraph 7 of the statement of claim, defendant denies that the correct amount of said overpayment was $8,807.90, but, on the contrary, alleges said overpayment was in truth and in fact $1,467.64. Defendant admits that said overpayment of $1,467.64 resulted from the determination of plaintiff's allowance for amortization of war-time facilities pursuant to section 234 (a) (8) of the revenue act of 1918 in the sum of $387,224.40. Defendant denies, however, that said determination was a redetermination, and denies that said allowance was at any time determined at $1,344,465.15, or any other sum than $387,224.40. On the contrary, defendant alleges said determination of the said amortization allowance at $387,224.40 was the only amortization allowance at any time actually determined by the Commissioner of Internal Revenue.

15 Defendant denies that plaintiff's allowance for the year 1919 as a deduction for said amortization was changed by any determination whatsoever from $99,016.94 to $18,202.10, but, on the contrary, defendant alleges that said allowance was determined only once (as provided by law) as above set forth and that, by said determination, plaintiff's claimed allowance of $99,016.94 was reduced to $71,267.51; and that said determination was in all respects correct, just, and legal.

8. In answer to the allegations contained in paragraph 8 of the statement of claim, defendant denies that said tax of $711,379.02, and/or the assessment and/or the collection thereof were in any sense erroneous, illegal, or void, except as to $1,467.64 thereof; but on the contrary alleges that said tax, its assessment, and its collection were in all respects correct, legal, and valid, except that $1,467.64 thereof constituted an overpayment (subsequently allowed to the plaintiff). Defendant denies that Exhibit I, attached to the statement of claim and made a part of it, is a correct statement of plaintiff's income and profits tax liability for the year 1919; denies that the exhibit shows the amount actually owing; and denies that it shows the amount of tax paid by the plaintiff in excess of the amount owing. On the

contrary, defendant alleges that the true amount of plaintiff's income and excess profits taxes for the year 1919 was $709.911.38, which was the sum lawfully assessed and actually collected from the plaintiff for said year.

16 9. In answer to the allegations contained in paragraph 9 of the statement of claim, defendant denies that at any time up to the third day of March, 1924, the amortization section of the Income Tax Unit and/or the employees thereof had full charge on the part of the Commissioner of Internal Revenue of the audit, investigation, and/or consideration of claims by taxpayers pursuant to section 234 (a) (8) of the revenue act of 1918, or section 234 (a) (8) of the revenue act of 1921 for allowance on account of amortization of war-time facilities. On the contrary, defendant alleges that, in truth and in fact, at all times the function performed by said amortization section was merely to make investigations, examinations, and recommendations as to the allowance of said claims; and that these recommendations were subject to further audit and review by the Bureau of Internal Revenue.

Defendant denies that at any time, the chief or acting chief of said section had any power or authority from the Commissioner of Internal Revenue to determine the amount of such allowances or to give notices of such determinations to claimants. Defendant also denies that said chief or acting chief of said section made such determination and/or gave such notices, either as a matter of routine or practice, or at all; or that said chief or acting chief did make such determination and/or give such notices, either with or without the knowledge, acquiescence, or approval of the said commissioner, or without consideration or action by the commissioner, personally.

17 On the contrary, defendant alleges that said chief and/or acting chief had no power or authority to determine the amount of such allowances; that the power to determine the allowable deductions under section 234 (a) (8) of the revenue act of 1918 and under section 234 (a) (8) of the revenue act of 1921 for amortization of war-time facilities was vested in the Commissioner of Internal Revenue at all times herein mentioned; that the report and recommendation of said amortization section was subject to audit and review by various audit and review sections of the Bureau of Internal Revenue; that before any allowance was actually made or became final and before said allowance became a determination pursuant to said sections of said revenue acts, respectively, said allowance and proposed determination was, both in theory and practice, subject to the approval of the Commissioner of Internal Revenue acting in person or through the assistant to the Commissioner of Internal Revenue. Defendant admits that, as a matter of practice and regular routine, notice of the report and recommendation of the amortization section was delivered to the plaintiff.

10. In answer to the allegations contained in paragraph 10 of the statement of claim, defendant admits that plaintiff constructed,

erected, installed, and acquired on or after April 6, 1917, certain buildings, machinery, equipment and other facilities for the production of articles contributing to the prosecution of the war with Germany, and at the time of filing its said return, plaintiff duly made claim for deduction from gross income under section 234 (a) (8) of the revenue act of 1918 on account of amortization of war-
18 time facilities, which claim was subsequently revised by the plaintiff, and the revised claim for $1,756,453.64 filed with the commissioner on or about September 10, 1921. Defendant denies that said sum of $1,756,453.64 was or is the correct amortization allowance to which plaintiff was, as a matter of fact, entitled and denies that $269,451.56 of plaintiff's allowable deduction was deductible from plaintiff's gross income for the year 1919. On the contrary, defendant alleges that, in truth and in fact, the correct amount of plaintiff's amortization allowance under said section was and is $387,224.40, of which $71,267.51 was deductible from plaintiff's gross income for the year 1919.

11. In answer to the allegations contained in paragraph 11 of the statement of claim defendant admits that in the month of September, 1921, the commissioner, acting by the authorized officials of said amortization section, sent his representative, one F. R. Griffith, an engineer in said amortization section, to the plaintiff's properties with written instructions and authority to examine the same, investigate the facts and matters set out in the plaintiff's said revised claim, audit said claim in the light of such investigation, and submit a report of the plaintiff's allowance under section 234 (a) (8) of the revenue act of 1918 to said amortization section. Defendant denies that said engineer was authorized or directed to make a determination of the amount of plaintiff's allowance for amortization under section 234 (a) (8) of the revenue act of 1918. On the contrary, defendant alleges that the sole power of said engineer
19 was to investigate and to report on the allegations contained in said claim.

12. In answer to the allegations contained in paragraph 12 of the statement of claim, defendant admits that said Griffith carried out his instructions and, on or about October 23, 1921, made a detailed report to said amortization section covering his said examination and investigation. Defendant denies that said Griffith ever made a determination of plaintiff's amortization allowance in any amount whatsoever and denies that said report constituted a determination that plaintiff was entitled to any allowance under said section 234 (a) (8) of the revenue act of 1918. On the contrary, defendant alleges that said report was merely a recommendation of said Griffith that plaintiff be allowed an amortization deduction in the amount of $1,344,465.15, of which $99,016.94 would be deductible from gross income for the year 1919.

13. In answer to the allegations contained in paragraph 13 of the statement of claim, defendant admits that in the ordinary and usual

course of business of the Income Tax Unit, said report came for review before one B. L. Wheeler, chief of engineers, in said amortization section; and admits that, upon such review and consideration thereof the said B. L. Wheeler approved said report and, on or about December 1, 1921, signified his approval in written endorsement thereon. Defendant denies that said B. L. Wheeler and/or said Griffith determined or were authorized to determine
20 plaintiff's amortization allowance in any sum whatsoever; denies that said report constituted a determination of plaintiff's amortization allowance; denies that any determination came on for review before said B. L. Wheeler; and denies that said B. L. Wheeler approved any determination thereof. On the contrary, defendant alleges said report was a mere recommendation which was approved by said B. L. Wheeler.

14. In answer to the allegations contained in paragraph 14 of the statement of claim, defendant admits that on or about the first day of December, 1921, in the ordinary and usual course of business of the Income Tax Unit, said report came on for review and action before one T. J. S. Kishpaugh, acting chief of said amortization section, and that said Kishpaugh then and there approved said report and signified his approval in written endorsement thereon. Defendant denies that said report constituted a determination of plaintiff's amortization allowance; denies that said report and/or any determination of plaintiff's amortization allowance came for final action before said Kishpaugh; denies that said Kishpaugh had any authority or power to make any determination or to take any final action relative to plaintiff's allowance with the same effect as if made by the Commissioner of Internal Revenue personally. On the contrary, defendant alleges: that said report constituted a mere recommendation relative to the amount of amortization allowance deductible by the plaintiff; that the action of said Kishpaugh was merely a concurrence in the recommendation thus previously
21 made; that said Kishpaugh had no power or authority on behalf of the Commissioner of Internal Revenue to take any final action relative to plaintiff's amortization allowance or to determine it; and that the action of said Kishpaugh was subject to further audit and review in the Bureau of Internal Revenue as herein above set forth.

15. In answer to the allegations contained in paragraph 15 of the statement of claim, defendant admits that a copy of said report with endorsements thereon, was delivered to plaintiff by said amortization section with the authority of the Commissioner of Internal Revenue. Defendant denies that said report was delivered on January 10th, 1922, and alleges it was delivered on or about December 2, 1921. Defendant denies that the correct deduction allowance to plaintiff on account of amortization of war-time facilities was $1,756,453.64. On the contrary, defendant alleges the correct amount

thereof was $387,224.40, which was in all respects fair and reasonable. Defendant denies that said report was accepted by plaintiff without further objection, and alleges that plaintiff expressed a willingness on numerous occasions, to accept it, provided its "case" could thereupon be closed. Defendant further alleges that said report appears upon its face to be merely a recommendation relative to plaintiff's amortization claims and to be subject to further audit and review; and that, at the time a copy of said report was delivered to the plaintiff, the plaintiff was advised that the report was subject to review and only a recommendation subject to the matters therein contained.

22 16. In answer to the allegations contained in paragraph 16 of the statement of claim, defendant denies that plaintiff never thereafter requested a further examination of its said returns with respect to said allowance. On the contrary, defendant alleges that plaintiff, thereafter, in briefs filed by it, requested the commissioner to make further adjustments in its said amortization allowance. Defendant admits that the commissioner did not thereafter, at any time prior to March 3, 1924, commence a reexamination of said returns with respect to said allowance, but defendant alleges that the first reexamination of said return with respect to said allowance was begun in the year 1921 and had not been completed on March 3, 1924, and was not completed until several years thereafter. Defendant denies that the commissioner did not determine that said allowance of $1,344,465.15 was erroneous and alleges that said amortization allowance was never determined at such sum. Defendant denies that the commissioner did not, subsequent to March 3, 1924, make further investigations and examinations and take further action with respect to plaintiff's amortization allowance. To the contrary, defendant alleges that plaintiff's said returns and plaintiff's claim for amortization allowance were continuously, from the year 1921 to a time long subsequent to March 3, 1924, in process of audit, investigation, and consideration. Defendant denies that no further proceedings were had or taken with respect to plaintiff's amortization allowance after said Griffith's report and the recommendation therein contained had been approved by said acting chief of the amortization section

23 in the amount of $1,344,465.15, on or about October 1, 1924. On the contrary, defendant alleges that said claim was continuously in process of audit as above set forth. Defendant further denies said report or its approval by said section officer constituted a determination and alleges that said allowance for amortization was not actually determined until it was approved and allowed by the assistant to the commissioner on, or about, July 11, 1927.

17. In answer to the allegations contiined in paragraph 17 of the statement of claim, defendant admits that on or about October 1, 1924, some person in the amortization section assigned the matter of plaintiff's claim for further examination. Defendant denies that

the claim was assigned for reexamination within the meaning of section 234 (a) (8) of the revenue act of 1918 or section 234 (a) (8) of the revenue act of 1921, and alleges that said further examination was a continuance of the audit thertofore begun. Defendant denies that no reexamination or reinvestigation was made, or begun, until on or about April 1, 1925, and alleges that the one and only reexamination and reinvestigation of plaintiff's return was commenced prior to March 3, 1924, and ended subsequently thereto. Defendant admits that one Luce, an engineer in said amortization section, made an investigation and examination of plaintiff's properties on or about April 1, 1925, and that on or about November 4, 1925, he made a report to said section covering his investigation and examination. Defendant denies said report was a determination of
24 any kind and alleges that (as appears on the face thereof) it was a mere recommendation regarding plaintiff's said claim to the effect that it be determined at $468,812.30; and that said report was subject to further review. Defendant admits that, on or about November 4, 1925, said amortization section sent to the plaintiff a copy of said report entitled "Redetermination of taxpayer's Claim for Amortization."

18. In answer to the allegations contained in paragraph 18 of the statement of claim, defendant admits that, on or about November 17, 1926, plaintiff received from said amortization section, a paper entitled "Second Redetermination of Amortization Claim." Defendant denies that plaintiff's said allowance was alleged therein to be determined at $378,224.40 (of which $369,022.30 was apportioned to the year 1918 and $18,202.10 to the year 1919). On the contrary, defendant alleges said report constituted a mere recommendation, and showed, on its face, that it was subject to further review.

19. In answer to the allegations contained in paragraph 19 of the statement of claim, defendant admits that the recommendation contained in said alleged and so-called "Second Redetermination" was approved by the commissioner and used by him in computing plaintiff's net income and tax for the year 1919, as stated in said letter of July 11, 1927. Defendant further alleges that the total deduction allowable for plaintiff for amortization of war-time facilities for the year 1919 was $71,267.51.

25 20. In answer to the allegations contained in paragraph 20 of the statement of claim, defendant denies that plaintiff is lawfully entitled to said amortization allowance in the sum of $1,344,465.15; denies that said allowance was in any way determined and/or allowed at such an amount; and denies that plaintiff is entitled to a deduction of $99,016.94 thereof from its 1919 gross income. On the contrary defendant alleges said allowance was correctly determined at $387,224.40 and that of the latter amount, plaintiff is entitled to a deduction of $71,267.51 from its gross income for the year 1919. Defendant denies that two "subsequent" redeterminations were made at all and alleges that only one determination was made as

herein above set forth in that plaintiff's claim was not finally determined until the action of the assistant to the commissioner on July 11, 1927, as herein above described. Defendant denies that the reports of the engineers of the amortization section constituted determinations within the purview of section 234 (a) (8) of the revenue act of 1918, or section 234 (a) (8) of the revenue act of 1921; and alleges that said reports were recommendations of the subscribers thereto and endorsers thereof that plaintiff's said claim be allowed in the amounts stated in said reports. Defendant denies that the report and recommendation upon which the commissioner based his determination of the amount of plaintiff's amortization allowance was not based on any new or material evidence or mathematical error or mistake. On the contrary, defendant alleges said report and the said determination were based on new and additional evidence;
26 that said Griffith erred in the recommendation made by him in his report; that his report was based on the assumed fact that several plant units of plaintiff were no longer required by plaintiff in the operation of its business, whereas, in truth and in fact, said plant units were but temporarily idle and were required by plaintiff in the operation of its business; that said investigation and report of F. R. Griffith was made during a period of temporary business depression and did not reflect the normal condition of plaintiff's business during the post-war period; that, upon field investigation subsequent to said Griffith's report, it was discovered that the cost upon which amortization had been recommended was greatly in excess of the true amount thereof.

21. In answer to the allegations contained in paragraph 21 of the statement of claim, defendant admits that on or about March 11, 1925, the plaintiff filed with the commissioner, a claim for refund of taxes paid for the year 1919. Defendant denies that said claim was for the sum of $8,807.90, and alleges that it was for the sum of $45,000.00. Defendant denies that said claim was filed on the ground that said tax and assessment and collection thereof were erroneous, illegal, and void to the extent of said alleged overpayment and avers that said claim was filed on the following grounds (reference therein being made to briefs thereafter to be filed by the plaintiff):

"This claim is filed as a protection against the running of the statute of limitations.

"The questions involved are affiliations, depreciation, deple-
27 tion, valuation of contracts and other items; also, relief under provisions of sections 327 and 328."

22. In answer to the allegations contained in paragraph 22 of the statement of claim, defendant admits that, except for $1,467.64 no further sums have been refunded to the plaintiff. It is denied, however, that plaintiff has overpaid its taxes for said year in any amount in excess of said refund heretofore made to the plaintiff.

FIRST SEPARATE DEFENSE

As a further and separate defense to the allegations contained in the statement of claim, defendant alleges that:

23. This court is without jurisdiction to review the action of the said commissioner in computing plaintiff's profits tax for the year 1919 under said sections 327 and 328.

24. This court is without jurisdiction to compute plaintiff's profits tax for the year 1919 at 18.31% of plaintiff's net income, as said income is sought to be revised by the allegations of the statement of claim.

SECOND SEPARATE DEFENSE

As a further and second separate defense to the allegations contained in the statement of claim, defendant, at this point incorporates herein the allegations of the "First separate defense" as fully as if here set forth in detail, and further alleges that:

28 25. The amounts of profits tax due from the plaintiff for the years 1918 and 1919, respectively, were computed by the Commissioner of Internal Revenue pursuant to the provisions of sections 327 and 328 of the revenue act of 1918; for the year 1919, plaintiff's profits tax was computed under said sections to be 18.31% of its net income for that year; that, if the income and/or invested capital found by the said commissioner to be plaintiff's true income and invested capital for said year are in any way modified by court action, then the profits tax due from the plaintiff for the year 1919 may not be computed under said sections 327 and 328 of the revenue act of 1918 by any court, but must be computed under section 301 of the revenue act of 1918, provided that the court has jurisdiction to compute them at all.

26. There is now pending in this court an action by this plaintiff, against D. B. Heiner, collector of internal revenue for the twenty-third district of Pennsylvania (No. 5762 law), wherein plaintiff seeks to recover $1,164,015.33, collected from it as income and excess profits taxes for the years 1918 and 1920, inclusive. Said suit is based, in part, upon an alleged erroneous redetermination of plaintiff's allowable deduction for amortization of war-time facilities and upon an alleged erroneous disallowance, in part, of plaintiff's claim for depreciation for said years. After plaintiff's return for 1918 had been filed, it filed a revised claim for amortization in the amount of $1,756,453.64. Thereafter, said claim was disallowed in the sum of $1,369,229.24 and allowed in the sum of $387,224.40. Plain-

29 tiff also then claimed, as a deduction from gross amount for the year 1918, depreciation in the amount of $876,366.71. Upon audit of plaintiff's said return, the commissioner disallowed depreciation in the sum of $439,104.16 and allowed said deduction for the balance. Plaintiff's invested capital was thereupon increased in the amount that said claims were disallowed, said amounts being restored to invested capital for the year 1919. If, in said action

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Nos. 476 - 477 - 478

In the Supreme Court of the United States

OCTOBER TERM, 1932

D. B. HEINER, COLLECTOR OF INTERNAL REVENUE FOR THE TWENTY-THIRD DISTRICT OF PENNSYLVANIA, PETITIONER

v.

DIAMOND ALKALI COMPANY, A CORPORATION

C. G. LEWELLYN, FORMERLY COLLECTOR OF INTERNAL REVENUE FOR THE TWENTY-THIRD DISTRICT OF PENNSYLVANIA, PETITIONER

v.

DIAMOND ALKALI COMPANY, A CORPORATION

PETITION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

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144590—32——1

In the Supreme Court of the United States

OCTOBER TERM, 1932

No. —

(Nos. 4419 and 4426 in the Circuit Court of Appeals)

D. B. HEINER, COLLECTOR OF INTERNAL REVENUE for the Twenty-third District of Pennsylvania, petitioner

v.

DIAMOND ALKALI COMPANY, A CORPORATION

No. —

(No. 4427 in the Circuit Court of Appeals)

C. G. LEWELLYN, FORMERLY COLLECTOR OF INTERNAL REVENUE for the Twenty-third District of Pennsylvania, Petitioner

v.

DIAMOND ALKALI COMPANY, A CORPORATION

PETITION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

The Solicitor General, on behalf of D. B. Heiner, Collector of Internal Revenue for the Twenty-third District of Pennsylvania, and C. G. Lewellyn, formerly Collector of Internal Revenue for that District, prays that writs of certiorari issue to review

the judgments of the Circuit Court of Appeals for the Third Circuit entered in the above causes on July 26, 1932, upon rehearing granted at the instance of the Diamond Alkali Company, affirming in part and reversing in part the judgments of the District Court for the Western District of Pennsylvania, 39 F. (2d) 645 (Nos. 4419 and 4426, B. of E., 1115; No. 4427, R. 86).[1]

OPINIONS BELOW

The findings of fact and conclusions of law of the District Court (Nos. 4419 and 4426, B. of E., 1072–1111; No. 4427, R. 69–82) are reported in 39 F. (2d) 645. The original opinion of the Circuit Court of Appeals appears at No. 4427, R. —, and the opinion of that court upon reargument appears at No. 4427, R. —. These opinions are not yet reported.

JURISDICTION

The judgments sought to be reviewed were entered on July 26, 1932. (Nos. 4419 and 4426, R. —; No. 4427, R.—.) The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the court below had the power to review the Commissioner's determination of the amount of the profits taxes due from the respondent where that determination was made pursuant to the discretion-

[1] The final Supreme Court records and case numbers not being available the record references herein are to the records in the Circuit Court of Appeals and are identified by the case numbers of that court. The bill of exceptions in Nos. 4419 and 4426 is printed separately, in three volumes.

ary powers confided to the Commissioner by Sections 327 and 328 of the Revenue Act of 1918.

STATUTES AND REGULATIONS INVOLVED

These are set forth in the Appendix, *infra*, pp. 13–17.

STATEMENT

The material facts, most of which were specially found by the District Court (Nos. 4419 and 4426, B. of E., 1072–1092; No. 4427, R. 69–81), are as follows:

The respondent filed income and profits tax returns for the years 1918 and 1919 and paid the taxes due as disclosed by these returns. Thereafter the respondent filed with the Commissioner an application for the computation of its 1918 and 1919 profits taxes under Sections 327 and 328 of the Revenue Act of 1918. The Commissioner granted this application (Nos. 4419 and 4426, B. of E., 1087; No. 4427, R. 375–376), having found that respondent's profits taxes, if determined without the benefit of Sections 327 and 328, would, owing to abnormal conditions affecting its capital or income, work upon it an exceptional hardship, evidenced by the gross disproportion between the tax as computed without the benefit of Section 327 and the tax computed by reference to the representative corporations specified in Sections 328.

In computing respondent's profits taxes under Section 328 the Commissioner determined the ratio of its tax to income for 1918 to be 54.54%, arriving at that ratio on the basis of the ratio of average tax

to average net income of representative corporations engaged in a like or similar trade or business. (Nos. 4419 and 4426, B. of E., 1088.) The ratio of tax to income for the year 1919 was determined by the Commissioner to be 18.31%. (Nos. 4419 and 4426, B. of E., 377; No. 4427, R. 80.) The Commissioner's computation for 1918 indicated a profits tax of $2,084,324.26 and an income tax of $206,039.99, a total tax liability of $2,290,364.25 (Nos. 4419 and 4426, B. of E., 377), whereas by computation of the tax under Section 301 of the 1918 Revenue Act (without special assessment) a profits tax of $2,592,789.30 and an income tax of $140,729.65, a total tax liability of $2,733,518.85, had been determined (Nos. 4419 and 4426, B. of E., 587). For 1919 the Commissioner determined respondent's excess-profits tax to be $709,926.02 together with an income tax of $192,634.09, a total of $902,560.11 (Nos. 4419 and 4426, B. of E., 608), under Section 301 of the Revenue Act of 1918 (without special assessment), whereas the computation under Section 328 showed a profits tax of $495,871.87 with income tax of $214,039.51, a total tax liability of $709,911.38 (Nos. 4419 and 4426, B. of E., 595). The taxes as determined by the Commissioner under Sections 327 and 328 were paid, but the respondent filed claims for refund of such taxes upon the ground that the Commissioner had erroneously disallowed certain deductions, and upon the rejection of said claims instituted these suits. Jury trials were waived in writing. (Nos. 4419 and 4426, B. of E., 3; No. 4427, R. 1.)

Respondent contended in the District Court that its taxable net income for 1918 and 1919 had been overstated by the Commissioner because of his failure to allow certain deductions for those years, and also that the Commissioner had erred in the application of Sections 327 and 328 in determining the ratio of tax to income for the year 1918 to be 54.54% when it should have been but 45%. It was neither charged nor proved that the Commissioner acted fraudulently or arbitrarily in determining the taxes under Sections 327 and 328.

The District Court held that the Commissioner had erred in failing to allow the claimed deductions to the extent of $238,001.09 for 1918 and $49,525.73 for 1919, and thereupon computed the profits taxes for each of said years at the ratio of the reduced net income for each year, which had previously been applied by the Commissioner (54.54% for 1918 and 18.31% for 1919) to the net income as computed by him. (Nos. 4419 and 4426, B. of E., 1089, 1091; No. 4427, R. 80.) Cross appeals were taken from the decision of the District Court with respect to the taxes for 1918, and the Collector appealed from the judgment with respect to the taxes for 1919.

The Circuit Court of Appeals held that the respondent was entitled to additional deductions from

income as follows (Nos. 4419 and 4426, R.—; No. 4427, R.—):

	Additional deductions allowed by Circuit Court of Appeals	Total additional deductions allowed by District Court and Circuit Court of Appeals
1918	$291,732.24	$528,733.33
1919	55,045.70	104,571.43

In its original opinion (Nos. 4419 and 4426, R. —; No. 4427, R. —) that court held that it was without power to review the Commissioner's computation of *profits* taxes under Sections 327 and 328, and allowed respondent a refund only with respect to its *income* taxes. But upon reargument the court held, Judge Thompson dissenting, that the rate (ratio) fixed by the Commissioner under Section 328 should be applied to the reduced net income of the respondent in computing the profits taxes.[2] (Nos. 4419 and 4426, R. —; No. 4427, R. —.)

SPECIFICATION OF ERRORS TO BE URGED

1. The Circuit Court of Appeals erred in undertaking to review the Commissioner's determination of respondent's profits taxes.

2. The Circuit Court of Appeals erred in holding that the application by it of the ratio determined by the Commissioner under the special assessment provisions of the statute, to a reduced net income fixed

[2] The court in its opinion upon the rehearing dealt also with the question of depreciation upon the unamortized cost of certain war facilities. That issue is not raised in this petition.

by the court, for the purpose of computing respondent's profits taxes, did not constitute a usurpation of the discretionary functions confided to the Commissioner by Sections 327 and 328.

3. The Circuit Court of Appeals erred in holding that the so-called "rates of tax" computed by the Commissioner under Section 328 should be applied to the reduced net income in computing respondent's profits taxes.

4. The Circuit Court of Appeals erred in affirming the District Court with reference to the issue of special assessment.

REASONS FOR GRANTING THE WRIT

1. The decision of the Circuit Court of Appeals conflicts with the principles announced in *Williamsport Wire Rope Co.* v. *United States*, 277 U. S. 551. This Court there held that discretionary power had been conferred on the Commissioner to determine whether or not taxpayers are entitled to the benefit of Sections 327 and 328, and also, if entitled to the benefits of those sections, the amount of the tax to be paid, and that such determinations are final and not subject to judicial review in the absence of fraud or similar irregularities. The Circuit Court of Appeals in the instant cases has not only undertaken to revise the Commissioner's determination in the absence of fraud or other irregularity, but has, in effect, undertaken to apply and give effect to Sections 327 and 328 and to exercise the functions which have been confided to the Commissioner. The decision of the Circuit Court of Appeals is probably

inconsistent with its own decisions in *Duquesne Steel Foundry Co.* v. *Commissioner*, 41 F. (2d) 995, affirmed *per curiam*, 283 U. S. 799, and *Cramer & King Co.* v. *Commissioner*, 41 F. (2d) 24. It is also at variance with the principles announced in *Brown's "Shamrock" Linens* v. *Bowers*, 48 F. (2d) 103 (C. C. A. 2d), certiorari denied, 283 U. S. 865, where it was held that the court had no jurisdiction to review the comparative data employed by the Commissioner in computing the tax, upon the mere allegation of error or illegality; *Standard Rice Co.* v. *Commissioner*, 41 F. (2d) 481 (C. C. A. 5th), ruling that the Board had fairly exercised its power of review of the Commissioner's denial of special assessment and that the court had no jurisdiction; *Oak Worsted Mills* v. *United States*, 38 F. (2d) 699 (C. Cls.), affirmed on other grounds, *sub nomine Graham & Foster* v. *Goodcell*, 282 U. S. 409, holding that the Commissioner is empowered to revise his determination of the tax computed by special assessment at any time within the statutory period; and *Cleveland Automobile Co.* v. *United States* (N. D. Ohio), not officially reported, discussing the jurisdiction of the courts to review an alleged overvaluation of inventory when the taxes were computed under the special assessment provisions of the Revenue Act of 1918. See also *Apollo Steel Co.* v. *Commissioner*, 41 F. (2d) 986 (C. C. A. 3d), certiorari denied, 282 U. S. 891; *Enameled Metals Co.* v. *Commissioner*, 42 F. (2d) 213 (C. C. A. 3d), affirmed *per curiam*, 283 U. S. 799; *Kehaha Sugar Co.* v. *Burnet*, 50 F. (2d)

322 (App. D. C.); *Railroad Supply Co.* v. *Burnet*, 51 F. (2d) 437 (App. D. C.).

2. The decision of the Circuit Court of Appeals is erroneous. In its initial opinion the court held that the District Court erred in redetermining the amount of the excess profits tax fixed by the Commissioner by applying the ratio of tax determined by the Commissioner to the reduced net income as determined by the court. In support of this view it invoked the *Williamsport Wire Rope Co.* case and also ~~in~~ *Brown's "Shamrock" Linens* v. *Bowers, supra.* In its subsequent decision the court abandoned its earlier view and, although conceding (No. 4427, R. —) the "bare possibility" that the reduction of net income might have some "conceivable effect" on the selection of the representative corporations contemplated by the special assessment provisions, held that the Commissioner could not, once having found the correct rate, apply it "to an incorrect and false income and produce an unjust tax." (No. 4427, R. —.) In an apparent effort to do what it conceived to be justice in the particular case, the court did indirectly what it could not do directly. The language of Sections 327 and 328, which refer to the *determining* and *computing* of the tax, makes it clear that Congress contemplated special assessment as a method of *computing the tax* and not merely a method of *fixing a rate.* In the *Williamsport Wire Rope Co.* case (pp. 558–559) the Court made it clear that the special functions vested in the

Commissioner by the statute extended to the "computation" of the tax "in all cases."

Moreover, the decision of the Circuit Court of Appeals amounts to an application of Section 328 without the performance of the preliminary tasks prescribed therein. The statute specifically defines the various factors which are to be employed by the Commissioner in the selection of comparatives and computation of the tax by means of special assessment. One of these factors is "net income," while another is "profits per unit of business transacted." The court can not disregard any one of these factors without affecting the result and in so doing it does precisely that which is not permitted under the statute. With the alteration in the taxpayer's net income the court sweeps away an indispensable factor upon which the Commissioner's computation was based. It may be that an entirely different group of comparatives would be selected by the Commissioner in view of such changes, and it is quite possible that with the reduction in net income the abnormality with respect to the respondent's capital and income might entirely disappear, together with all justification for allowing special assessment.

The decision of this Court in *Blair* v. *Oesterlein Machine Co.*, *supra*, established that the discretionary authority of the Board of Tax Appeals in matters of special assessment is coextensive with that vested in the Commissioner. The fact that the discretion of the Commissioner is subject to review by the Board

is believed to constitute a sufficient safeguard for the taxpayer who seeks the privilege of special assessment,[3] in view of the fact that the taxpayer may appeal to the courts in case of "fraud or other irregularities." *Williamsport Wire Rope Co.* v. *United States*, 277 U. S. 551, 562. Furthermore, where application has been made for special assessment and the Commissioner fixes a net income in excess of that returned by the taxpayer, it is customary to afford the taxpayer an opportunity to withdraw his request for special assessment.[4] Cf. *Chalmers Publishing Co.* v. *Commissioner*, 1 B. T. A. 629.

There is nothing in the record to warrant the conclusion that the action of the court below was based upon fraud or other irregularity on the part of the Commissioner. The courts have consistently recognized that this exception imports action by the Commissioner which is plainly arbitrary or involves a

[3] The respondent, by failing to seek a review before the Board, waived that right. This Court has held that the determinations of the Board, with reference to assessment under Section 328, are not reviewable in the courts. The same reasons require a holding that the Commissioner's determinations are final when no review is sought before the Board.

[4] It has not been established that the taxes were overpaid. At our request the Bureau of Internal Revenue has computed the profits taxes which would be due under the application of the normal method of Sec. 301 to the net income and invested capital as revised by the allowances in respect of depreciation and amortization granted by the court below. This shows that under such normal computation a difference of $37,143.31 for 1918 and $181,805.91 for 1919 would result in favor of the Government, as compared with the taxes as fixed by the Commissioner under special assessment.

clear abuse of discretion. Mere error upon the part of the Commissioner is not sufficient. *Live Stock Nat. Bank* v. *United States*, 36 F. (2d) 334 (C. C. A. 8th), certiorari denied, 281 U. S. 760; *National Bank of Commerce* v. *United States*, 39 F. (2d) 434 (C. C. A. 9th); *Ennis Coal Co.* v. *United States*, 37 F. (2d) 574 (C. C. A. 4th).

3. The question presented is involved in a considerable number of cases now pending involving taxes in the aggregate in excess of $3,000,000. Furthermore, the finality of the determination of the Commissioner, where made pursuant to statutes conferring upon him broad administrative powers involving the exercise of his discretion, is a matter which is of general importance in administering the taxing laws. While the taxing Act here involved is that of 1918, in its broader aspect the question is involved in other phases of the administration of later Revenue Acts in connection with the discretionary powers confided to the Commissioner.

Wherefore, it is respectfully submitted that this petition should be granted.

THOMAS D. THACHER,
Solicitor General.

OCTOBER, 1932.

APPENDIX

STATUTES AND REGULATIONS INVOLVED

Revenue Act of 1918, c. 18, 40 Stat. 1057, 1093:

SEC. 327. That in the following cases the tax shall be determined as provided in section 328:

* * * * *

(d) Where upon application by the corporation the Commissioner finds and so declares of record that the tax if determined without benefit of this section would, owing to abnormal conditions affecting the capital or income of the corporation, work upon the corporation an exceptional hardship evidenced by gross disproportion between the tax computed without benefit of this section and the tax computed by reference to the representative corporations specified in section 328. This subdivision shall not apply to any case (1) in which the tax (computed without benefit of this section) is high merely because the corporation earned within the taxable year a high rate of profit upon a normal invested capital, nor (2) in which 50 per centum or more of the gross income of the corporation for the taxable year (computed under section 233 of Title II) consists of gains, profits, commissions, or other income, derived on a cost-plus basis from a Government contract or contracts made between April 6, 1917, and November 11, 1918, both dates inclusive.

SEC. 328. (a) In the cases specified in section 327 the tax shall be the amount which bears the same ratio to the net income of the taxpayer (in excess of the specific exemption of $3,000) for the taxable year, as the average tax of representative corporations engaged in

a like or similar trade or business, bears to their average net income (in excess of the specific exemption of $3,000) for such year. In the case of a foreign corporation the tax shall be computed without deducting the specific exemption of $3,000 either for the taxpayer or the representative corporations.

In computing the tax under this section the Commissioner shall compare the taxpayer only with representative corporations whose invested capital can be satisfactorily determined under section 326 and which are, as nearly as may be, similarly circumstanced with respect to gross income, net income, profits per unit of business transacted and capital employed, the amount and rate of war profits or excess profits, and all other relevant facts and circumstances.

(b) For the purposes of subdivision (a) the ratios between the average tax and the average net income of representative corporations shall be determined by the Commissioner in accordance with regulations prescribed by him with the approval of the Secretary.

* * * * *

(c) The Commissioner shall keep a record of all cases in which the tax is determined in the manner prescribed in subdivision (a), containing the name and address of each taxpayer, the business in which engaged, the amount of invested capital and net income shown by the return, and the amount of invested capital as determined under such subdivision. The Commissioner shall furnish a copy of such record and other detailed information with respect to such cases when required by resolution of either House of Congress, without regard to the restrictions contained in section 257.

Treasury Regulations 45:

ART. 901. *Treatment of special cases.*—In the cases specified in section 327 of the statute the tax will be specially determined under the provisions of section 328, but the tax will not ordinarily be computed under section 328 merely because the corporation's form or manner of organization, or the limitations imposed by section 326, result in a greater tax than would otherwise be payable. A corporation which comes within the provisions of subdivision (d) of section 327 may make application for assessment under the provisions of section 328, which application shall be attached to its return in the form of a statement setting forth in full: (a) the reasons why the tax should be so determined; (b) the facts upon which such reasons are based; (c) an exact description of each trade or business or important branch of a trade or business carried on by it; (d) a statement of the invested capital and net income for each year since the beginning of the pre-war period; and (e) a statement showing the amount of gains, profits, commissions, or other income derived on a cost-plus basis from Government contracts made after April 5, 1917, and before November 12, 1918, and showing the per cent which such income is of the total income of the corporation. See sections 1 and 326 and Articles 831–871 and 1510.

ART. 911. *Computation of tax in special cases.*—In the cases specified in section 327 of the statute the tax is to be computed by comparison with representative corporations whose invested capital can be satisfactorily determined under section 326 and which are engaged in a like or similar trade or business and similarly circumstanced. The provisions of section 328 do not permit the determination of a general average for any trade or

business. In each case which comes under the provisions of section 327 the Commissioner will determine, as nearly as may be, the group or class of corporations with which the corporation should be compared and the amount which bears the same ratio to the net income of the corporation (in excess of the specific exemption of $3,000) for the taxable year as the average tax of such representative corporations bears to their average net income (in excess of the specific exemption of $3,000) for such year. The comparison will take account of similarity with respect to gross income, net income, profit per unit of business transacted and capital employed, the amount and rate of war profits or excess profits, and all other relevant facts and circumstances.

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FILE COPY

Nos. 476, 477, and 478

In the Supreme Court of the United States

OCTOBER TERM, 1932

D. B. HEINER, COLLECTOR OF INTERNAL REVENUE FOR THE TWENTY-THIRD DISTRICT OF PENNSYLVANIA, PETITIONER

v.

DIAMOND ALKALI COMPANY, A CORPORATION

C. G. LEWELLYN, FORMERLY COLLECTOR OF INTERNAL REVENUE FOR THE TWENTY-THIRD DISTRICT OF PENNSYLVANIA, PETITIONER

v.

DIAMOND ALKALI COMPANY, A CORPORATION

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE PETITIONERS

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In the Supreme Court of the United States

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D. B. HEINER, COLLECTOR OF INTERNAL REVENUE for the Twenty-third District of Pennsylvania, petitioner

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DIAMOND ALKALI COMPANY, A CORPORATION

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v.

DIAMOND ALKALI COMPANY, A CORPORATION

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE PETITIONERS

OPINIONS BELOW

The findings of fact and conclusions of law of the District Court in Nos. 476 and 477 (R. 81–91) are

reported in 39 F. (2d) 645. That Court's findings of fact and conclusions of law in No. 478 (R. 27–34) are not reported.[1] The original opinion of the Circuit Court of Appeals (Nos. 476 and 477, R. 106–116) and its opinion on rehearing (Nos. 476 and 477, R. 125–129) are reported in 60 F. (2d) 505.[2]

JURISDICTION

The judgments of the Circuit Court of Appeals were entered July 26, 1932. (Nos. 476 and 477, R. 129, 130; No. 478, R. 62.) Petition for writs of certiorari was filed October 26, 1932, and writs were granted December 5, 1932. (Nos. 476 and 477, R. 133; No. 478, R. 65.) Jurisdiction is conferred upon this Court by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

---

[1] The *Heiner case*, Nos. 476 and 477 (No. 4419 and 4426 in the Circuit Court of Appeals), relates to respondent's taxes for 1918. In that case two judgments, in identical terms, were entered by the court below, one disposing of the taxpayer's appeal, and the other disposing of the cross-appeal of the Collector. The *Lewellyn case*, No. 478 (No. 4427 in the Circuit Court of Appeals), relates to taxes for 1919.

The *Heiner case* in the courts below also involved taxes for 1920. The allowance by the Circuit Court of Appeals of additional amortization deductions for 1918 and 1919 will operate to reduce respondent's invested capital for 1920 and will thus affect the amount of the 1920 taxes. This matter, of course, may be adjusted upon the return of the case to the District Court.

[2] By stipulation of the parties there has been omitted from the printed record in this Court portions of the record in the court below which dealt with issues not here presented.

QUESTION PRESENTED

The Commissioner determined respondent's profits taxes for 1918 and 1919 by special assessments under Sections 327 and 328 of the Revenue Act of 1918. Upon suits for refund against the Collector, the District Court and the Circuit Court of Appeals upon appeal allowed respondent certain additional deductions from gross income, the effect of which was correspondingly to reduce the amount of the respondent's net income for each of the years 1918 and 1919. The questions here presented are:

(1) Whether the courts below had the power to set aside and review the Commissioner's determination of the amount of *profits taxes* due from respondent.

(2) If so, whether the courts below had the power to redetermine such taxes by applying to the reduced net income the ratios of tax to net income previously used by the Commissioner in his special assessments.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in Appendix A, pp. 35–40, *infra*.

STATEMENT

The respondent duly filed income and profits tax returns for the years 1918 and 1919 and paid the income and profits taxes due as disclosed by these returns in the respective amounts of $1,074,749.11

and $711,392.02. Thereafter the respondent filed with the Commissioner an application for the computation of its 1918 profits taxes under Sections 327 and 328 of the Revenue Act of 1918.[3] (Nos. 476 and 477, R. 89.) The Commissioner granted this application, having found that the respondent's excess profits tax for 1918 as determined without the benefit of Section 327 of the Revenue Act of 1918 would, owing to abnormal conditions affecting capital or income, work upon the respondent an exceptional hardship, evidenced by gross disproportion between the tax computed without the benefit of Section 327 and the tax computed by reference to the representative corporations specified in Section 328 of the Revenue Act of 1918. (Nos. 476 and 477, R. 89.)

In computing respondent's profits tax for 1918 under Section 328 the Commissioner determined the ratio of tax to net income at 54.54 per cent, arriving at that ratio, as he claimed, on the basis of the ratio of average tax to average net income of representative corporations engaged in a like or

[3] On December 23, 1925, the Commissioner advised the respondent that before its application could be granted there must be "a final determination of your tax liability computed on the basis of statutory invested capital," and granted the respondent thirty days in which to protest "against the determination of your net income and statutory invested capital as shown in the attached statement." It does not appear that such a protest was filed. But see footnote 13, p. 17, *infra*.

similar trade or business. (Nos. 476 and 477, R. 89.) By this computation the Commissioner determined, upon a net income found by him to be $3,821,143.63, a profits tax of $2,084,324.26 and an income tax of $206,039.99, a total tax liability of $2,290,364.25 (Nos. 476 and 477, R. 69–76), whereas a computation of respondent's taxes under Section 301 of the Revenue Act of 1918, i. e., without special assessment, upon a net income of $3,785,355.05 had indicated a profits tax of $2,592,789.30, and an income tax of $140,729.65, a total tax liability of $2,733,518.85. (Nos. 476 and 477, R. 80.)

On application by the respondent the Commissioner also granted special assessment for 1919[4] and computed the profits tax for that year by a like method (Nos. 476 and 477, R. 71), finding a ratio of tax to net income of 18.31 per cent (No. 478, R. 33). By this computation the Commissioner determined for 1919, upon a net income of $2,708,248.07, a profits tax of $495,871.87 and an income tax of $214,039.51, a total tax of $709,911.38 (Nos. 476 and 477, R. 72), whereas a computation without special assessment had indicated a profits tax of $709,926.02 and an income tax of $192,634.09, a total tax of $902,560.11. (Nos. 476 and 477, R. 64.)

The taxes as determined by the Commissioner were paid (Nos. 476 and 477, R. 83) but the respondent filed claims for refund of a portion

[4] The application for 1919 was at first denied. (Nos. 476 and 477, R. 62.)

thereof,[5] which claims were rejected by the Commissioner (Nos. 476 and 477, R. 89). Thereafter the instant suits were instituted by the respondent. Jury trials were waived in writing. (Nos. 476 and 477, R. 52; No. 478, R. 28.)

The respondent contended in the District Court that its net income for 1918 and 1919 had been overstated by the Commissioner because of his failure to allow certain deductions for amortization and depreciation. (Nos. 476 and 478, R. 3–4.) Respondent further contended that the Commissioner had erred in the application of Section 328 of the Revenue Act of 1918 to its taxes for 1918 by determining the ratio of profits tax to net income to be 54.54 per cent when, as respondent contended, it should have been 45 per cent. (Nos. 476 and 477, R. 7.) It was neither alleged nor proved that the Commissioner acted fraudulently or arbitrarily in determining the profits taxes for 1918 and 1919 under Sections 327 and 328.

The District Court allowed additional deductions from gross income of $238,001.09 for 1918 and $49,525.73 for 1919, and thereupon recomputed the profits taxes for each of these years by applying to the reduced income the ratios of 54.54% and 18.31%, respectively, which had been used by the

[5] The claim as to 1918, which is the only one appearing in the record (Nos. 476 and 477, R. 57–59), was predicated partly upon the ground that the Commissioner had erroneously failed to allow respondent certain deductions from gross income.

Commissioner upon the net income as computed by him at the time of his determination of the taxes by special assessment. (Nos. 476 and 477, R. 90; No. 478, R. 33.) Cross appeals were taken from the decision of the District Court with respect to the year 1918, and the Collector appealed from the judgment for 1919.

In its original opinion the Circuit Court of Appeals held that the respondent was entitled to still further deductions from gross income, increasing the additional deductions allowed by the District Court by $236,229.18 for 1918 and by $55,045.70 for 1919.[6] In its opinion on reargument the court further increased the deductions for 1918 by granting an additional depreciation allowance of $55,503.06.[7] (Nos. 476 and 477, R. 128.)

In its original opinion the Circuit Court of Appeals held that the District Court was in error in

[6] While the allowance of an increased deduction for 1919 was not relied upon by the petitioners as a reason for granting certiorari, the action of the Circuit Court of Appeals in this respect was clearly erroneous since the taxpayer did not appeal from the judgment of the District Court for that year.

[7] The additional deductions allowed by the Courts below were as follows:

Year	Allowed by District Court	Allowed by Circuit Court of Appeals	Total additional deduction
1918	$238,001.09	$291,732.24	$529,733.33
1919	49,525.73	55,045.70	104,571.43

redetermining the amounts of the excess profits taxes fixed by the Commissioner and held that the respondent was entitled to a refund only with respect to its income taxes. (Nos. 176 and 177, R. 115-116.) Upon reargument the court held, Judge Thompson dissenting, that the respective rates (ratios) fixed by the Commissioner under Section 328 should be applied to the reduced net income for the years in question in computing the profits taxes for those years. (Nos. 176 and 177, R. 125-127.)

SPECIFICATIONS OF ERROR

The Circuit Court of Appeals erred

1. In undertaking to review the Commissioner's determination of respondent's profits taxes.

2. In holding that its applying the ratio determined by the Commissioner under the special assessment provisions of the statute to a reduced net income fixed by the court, for the purpose of computing respondent's profits taxes, did not constitute a usurpation of the discretionary functions confided to the Commissioner by Sections 327 and 328 of the Revenue Act of 1918.

3. In holding that the so called "rates of tax" computed by the Commissioner under Section 328 should be applied to the reduced net income in computing respondent's profits taxes.

4. In affirming the judgment of the District Court with reference to the issue of special assessment.

SUMMARY OF ARGUMENT

I

The courts below were without authority to review and set aside the Commissioner's determination to levy special assessment of respondent's profits taxes. The considerations which determine the right to receive special assessment under Section 327 (d) of the Revenue Act of 1918 "and those which govern the computation in all cases" are the ordinary functions of the Commissioner, and the courts may not review his exercise of those functions in the absence of fraud or like irregularity.

In the instant case there is no allegation or proof of fraud, and no "irregularity" is suggested other than that the Commissioner's computations of the taxes were predicated upon the mistaken finding that respondent's net income was greater than it actually was. The failure of the Commissioner to allow certain deductions from gross income was a mere error with respect to the propriety of the deductions and did not represent such essentially arbitrary action on his part as would warrant a judicial review of the special assessments.

Having elected to seek relief in the courts, the respondent has necessarily precluded a review of those portions of the Commissioner's determination which do not present justiciable questions.

Assuming that the courts below possessed authority to review and set aside the Commissioner's determination of the profits taxes by special assessment, they were without authority to recompute the taxes by applying to the reduced net income the ratios of tax used by the Commissioner in connection with a greater net income. Such ratios were found by comparison of respondent with representative corporations similarly situated "with respect to gross income, net income, profits per unit of business transacted * * * and all other relevant facts and circumstances." The amount of respondent's net income was necessarily a basic factor in the selection of the comparative corporations. Because of the substantial alteration of such basic factor it is impossible to know whether the respondent still was entitled to special assessment, and, if so, what the correct ratios of tax to income should be. Moreover, neither the granting of a new special assessment nor the recomputation of the taxes could be made without performance of the preliminary tasks required of the Commissioner by the statute. In computing new special assessments without the performance of such preliminary tasks, the court below not only exceeded its authority but it necessarily made erroneous determinations.

Assuming that respondent's profits taxes might be redetermined by the courts below, the power of the courts was limited to a redetermination of such taxes *without special assessment*, i. e., under Section 301 of the statute. In the instant cases there was no room for the operation of this limited jurisdiction since the respondent conceded in the court below that its profits taxes as computed on its reduced net income without special assessment would be greater in amount than the taxes as computed by the Commissioner.

ARGUMENT

I

THE COURTS BELOW WERE WITHOUT AUTHORITY TO REVIEW AND SET ASIDE THE COMMISSIONER'S DETERMINATION BY SPECIAL ASSESSMENT OF RESPONDENT'S PROFITS TAXES IN THE ABSENCE OF FRAUD OR LIKE IRREGULARITY

The petitioners contend that the action of the Circuit Court of Appeals in setting aside the Commissioner's determination of respondent's profit taxes and in redetermining such taxes constituted a review of the Commissioner's determination which was unauthorized by the statute and beyond the power of the court. They contend further that in recomputing the profits taxes, by applying to the reduced net income the ratios determined by the Commissioner upon a different net income, the court below *made new special assessments*, and

thus usurped discretionary functions entrusted to the Commissioner.[8]

It is definitely settled that both the determination whether special assessment shall be accorded a taxpayer[9] under Sections 327 and 328 of the Revenue Act of 1918 and the computation of the tax by special assessment[10] are matters within the discretionary powers of the Commissioner, and that

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[8] Petitioners do not question here the action of the courts below in reducing the *normal income tax* by increasing the deductions from gross income and applying to the reduced net income the normal tax rate prescribed by the statute. The questions presented to this Court in the instant cases relate only to the *profits taxes*. Attention, however, is called to the fact that there is a necessary correlation between the profits tax and the income tax since, under Sec. 236 (b) of the statute, the amount of the former is allowed as a credit against net income in computing the latter.

[9] *Williamsport Wire Rope Co.* v. *United States*, 277 U. S. 551, *supra; Duquesne Steel Foundry Co.* v. *Commissioner*, 41 F. (2d) 995 (C. C. A. 3d), affirmed *per curiam*, 283 U. S. 799; *Enameled Metals Co.* v. *Commissioner*, 42 F. (2d) 213 (C. C. A. 3rd), affirmed *per curiam*, 283 U. S. 799. See *Oak Worsted Mills* v. *United States*, 38 F. (2d) 699 (C. Cls.), affirmed on other grounds, 282 U. S. 409; *Standard Rice Co.* v. *Commissioner*, 41 F. (2d) 481 (C. C. A. 5th); *Cramer & King Co.* v. *Commissioner*, 41 F. (2d) 24 (C. C. A. 3d); *Kekaha Sugar Co.* v. *Burnet*, 50 F. (2d) 322 (App. D. C.); *Railroad Supply Co.* v. *Burnet*, 51 F. (2d) 437 (App. D. C.). See also *United States* v. *Henry Prentiss & Co., Inc.*, No. 234, present term, decided January 9, 1933.

[10] *Brown's "Shamrock" Linens* v. *Bowers*, 48 F. (2d) 103 (C. C. A. 2d), certiorari denied, 283 U. S. 865; *Chicago Frog & Switch Co.* v. *United States*, 67 C. Cls. 662, certiorari denied, 280 U. S. 579. In the *Brown's "Shamrock" Linens* case the taxpayer was a foreign corporation and as such was automatically entitled to special assessment.

the courts may not review his exercise of these functions in the absence of fraud or like irregularity.

In *Williamsport Wire Rope Co.* v. *United States*, 277 U. S. 551, *supra*, the Court said (pp. 558–559, 560, 562):

> The task imposed on the Commissioner by §§ 327 and 328 was one that could only be performed by an official or a body having wide knowledge and experience with the class of problems concerned. For the requirement of a special assessment under paragraph (d) of § 327 *and its computation in all cases*, are dependent on "the average tax of representative corporations engaged in a like or similar trade or business."
>
> To perform that task, power discretionary in character was necessarily conferred. Whether, as provided in paragraph (d) of § 327, there are "abnormal conditions;" whether there would be "gross disproportion" between the tax computed under § 301 and "that computed by reference to the representative corporations specified in section 328;" what are "representative corporations engaged in a like or similar trade or business;" which corporations are "as nearly as may be, similarly circumstanced with respect to gross income, net income, profits per unit of business transacted and capital employed, the amount and rate of war profits or excess profits, and all other relevant facts and circumstances"—these

> are all questions of administrative discretion.
>
> * * * * *
>
> Thus the aims which induced Congress to enact §§ 327 and 328, the nature of the task which it confided to the Commissioner, the methods of procedure prescribed, and the language employed to express the conditions under which the special assessment is required, *all negative the right to a review of his determination by a court.*
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> * * * * *
>
> We conclude that the determination whether the taxpayer is entitled to the special assessment was confided by Congress to the Commissioner, and could not, under the Revenue Act of 1918, be challenged in the courts—at least in the absence of fraud or other irregularities. (Italics ours.)

The *Williamsport case* and other cases above cited leave no room for doubt that the question whether respondent was entitled to special assessment under Section 327 (d) and the computation of the tax under Section 328 were matters which were beyond the jurisdiction of the courts below to review—"at least in the absence of fraud or other irregularities." In the instant cases there is no allegation or proof of fraud, and no irregularity is here suggested other than that the Commissioner's computation of the tax was predicated upon the mistaken finding that respondent's net

income was greater than it actually was. The courts have consistently recognized that the words "fraud or other irregularities" as used in the *Williamsport case* import action on the part of the Commissioner which is essentially arbitrary or which involves a clear abuse of discretion. Mere error on his part is not sufficient. *Live Stock Nat. Bank* v. *United States,* 36 F. (2d) 334 (C. C. A. 8th); *National Bank of Commerce* v. *United States,* 39 F. (2d) 434 (C. C. A. 9th). Obviously the fact that the Circuit Court of Appeals allowed respondent additional deductions from gross income does not demonstrate that the Commissioner's special assessments were fraudulent or arbitrary.

In its brief in opposition to the petition for certiorari, the respondent argued that the result contended for by the Government is unjust, and that its necessary effect is to make the Commissioner the sole judge as to what constitutes income and what deductions a taxpayer may take.[11] This argument is predicated upon the assumption that if the Commissioner had been aware of respondent's

[11] In its brief in opposition respondent says (pp. 9–10): "Carried to its logical conclusion the petitioners' contention means that if the court had found that the Diamond Alkali Company had, for example, only $1,000,000 of net income or even none, the profits tax must remain at more than $2,000,000."

We think the conclusion thus imputed to petitioners is neither logical nor the one to which their contention leads. The words "other irregularities" as used in the *Williamsport case* were intended to have some operation, and the

correct net income he would still have found that it was entitled to special assessment for the years in question, and on the further assumption that the taxes as computed on the reduced net income would be less than the taxes as originally computed by the Commissioner. But these assumptions are not well founded. The reduction of respondent's net income in a substantial amount might well have eliminated the need for special assessment, or required the selection of new comparative corporations for the purpose of determining that need, or resulted in the selection of comparatives having a higher ratio of tax to net income.

The Commissioner computed the profits taxes by special assessment only because respondent requested it. A condition precedent to the computation of profits taxes by special assessment is the prior determination of the taxpayer's net income; otherwise the application for special assessment would be wholly academic, and no such assessment could be made. Accordingly, neither the necessity for special assessment nor the amount of the tax can be determined, with final effect upon the tax liability, except where the parties are agreed upon

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determination and assessment by the Commissioner of a profits tax in excess of the taxpayer's net income might well present a result so unjust and extreme as to require the judicial review otherwise denied. The instant cases present no such situation. Indeed, respondent conceded in the court below that its profits taxes, as computed by the Commissioner, are less than such taxes would be if computed without special assessment on its net income *as reduced* by the courts below. (See p. 31, *infra*.)

the amount of the net income.[12] Taxpayer's obtaining special assessment is wholly inconsistent with its later effort to have its net income reduced.[13] As this Court recently pointed out with respect to the statute here involved in *United States* v. *Henry Prentiss & Co., Inc.*, No. 234, present term, decided January 9, 1933:

> The presentation of such a claim [for special assessment], unlike the presentation of a claim of error in fact or law, does not suggest the need for a new and general audit of assets and liabilities. The two proceed-

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[12] In special assessment cases it is customary, as was done in this case (Nos. 476 and 477, R. 75–76), to request an acquiescence by the taxpayer in the amount of income and invested capital. See *United States* v. *Henry Prentiss & Co., Inc., supra.*

[13] By its letter of December 23, 1925 (Nos. 476 and 477, R. 75–80), the Bureau advised the respondent that its request for special assessment for 1918 could not be considered until final determination of its tax liability computed on the basis of invested capital, and the respondent was given 30 days to protest against the Commissioner's determination of net income (Nos. 476 and 477, R. 76) and invested capital. The record does not disclose that such a protest was made. It does appear that thereafter, by his letter of March 19, 1927, the Commissioner changed his determination of respondent's 1918 net income by *increasing* it. (Nos. 476 and 477, R. 61.) The respondent apparently filed a protest against this determination (Nos. 476 and 477, R. 70) which was overruled by the Commissioner's final letter of July 11, 1927 (Nos. 476 and 477, R. 69–73). This was the final determination of the Commissioner from which taxpayer was entitled to appeal to the Board of Tax Appeals. Substantially the same steps seem to have been followed by both respondent and the Commissioner with respect to the 1919 taxes. (Nos. 476 and 477, R. 60, 69.)

> ings, alike in form and in consequences, *are essentially diverse* * * *. The grievances differ so essentially that the assertion of *the one must be felt to be unrelated to any complaint* as to the other. (Italics ours.)

Substantially the same idea was expressed in a manner specifically applicable to the instant cases in *Cleveland Automobile Company* v. *United States* (N. D. Ohio), decided February 24, 1932, not reported officially, where the court said (Prentice-Hall Federal Tax Service, 1932, Vol. 1, p. 897, 900):

> In this action it [the taxpayer] seeks to have the Court reduce its income and redetermine its profits tax liability computed under special assessment on the basis of the reduced income. * * * If the net income determination never is to become final until the taxpayer is satisfied with the resulting tax liability, the nature and aims of the relief provided by Sections 327 and 328 * * * are to no purpose.

The relief sought under Section 327 (d) differs widely in its form and method of determination from the normal statutory method of computing profits taxes. In one application is addressed to the discretionary judgment of an administrative official, while the other is controlled by the terms of the statute. The remedy in one case is administrative; in the other a justiciable question is presented. We think it was incumbent upon the

respondent, in view of the inherent differences between special assessment and the normal computation of profits taxes, to elect the path it would follow. From the very nature of special assessment and the inability of the courts to control or review the administrative determination, when the taxpayer appeals to the judicial branch he abandons the right further to contest the validity of the administrative determination made at his request. The election is unavoidable because the taxpayer cannot raise a nonjusticiable question in a judicial proceeding. See *Cleveland Automobile Co.* v. *United States* (N. D. Ohio), decided February 24, 1932, *supra*.

We submit that the courts below erred in reviewing and setting aside the Commissioner's determination of respondent's profits taxes.

II

THE COURTS BELOW WERE WITHOUT AUTHORITY TO REDETERMINE RESPONDENT'S PROFITS TAXES BY APPLYING TO THE REDUCED NET INCOME THE SPECIAL ASSESSMENT RATIOS DETERMINED BY THE COMMISSIONER

It does not follow that because respondent's net income was reduced the profits taxes as determined by the Commissioner exceeded the amounts properly due on the reduced net income. (See pp. 15–16, *supra*; pp. 22–25, *infra*.) But even if it be held that, since the Commissioner's special assessments were based upon net incomes in excess of those fixed by the courts below, the respondent's

profits taxes as well as its normal income taxes must be redetermined, the courts below lacked the power to recompute the profits taxes by applying the Commissioner's special assessment ratios to the reduced net income.

The respondent's right to special assessments is predicated upon subdivision (d) of Section 327. (Nos. 476 and 477, R. 89.) That subdivision provides that profits taxes shall be determined by special assessment where, on application by a corporation, the Commissioner finds and declares that the tax if determined without benefit of special assessment would, owing to abnormal conditions affecting capital or income, work upon the corporation an exceptional hardship evidenced by gross disproportion between the tax computed without the benefit of special assessment and the tax computed under Section 328 with reference to the average tax of representative corporations." Section 328 (a) provides that in cases specified in Section 327 the tax shall be the amount "which bears the same ratio to the *net income* of the taxpayer" as the "average tax of representative corporations engaged in a like or similar trade or business, bears to their average *net income*." (Italics ours.) Section 328 (a) further provides:

"The primary purpose underlying the enactment of these provisions was to afford relief in those exceptional cases where the normal method of determining profits taxes would result in grave hardships or serious inequality. See Sen. Rept. No. 617, 65th Cong., 3rd Sess., pp. 14–15.

> * * * the Commissioner shall compare the taxpayer only with representative corporations * * * which are, as nearly as may be, similarly circumstanced with respect to gross income, net income, profits per unit of business transacted and capital employed, the amount and rate of war profits or excess profits, and all other relevant facts and circumstances.

Section 328 (b) provides that "the ratios between the average tax and the average net income of representative corporations" shall be determined by the Commissioner in accordance with regulations prescribed by him. Article 911, Treasury Regulations 45 (1920 Edition), issued under the Revenue Act of 1918, pp. 37–38, *infra*, provides in part:

> The provisions of section 328 do not permit the determination of a general average for any trade or business. In each case which comes under the provisions of section 327 the Commissioner will determine, as nearly as may be, the group or class of corporations with which the corporation should be compared * * *.

The ratios used by the Commissioner in computing respondent's profits taxes for 1918 and 1919 by special assessment were found by comparison of respondent with representative corporations similarly situated "with respect to gross income, *net income, profits per unit of business transacted*

and capital employed, the amount and rate of war profits or excess profits, *and all other relevant facts and circumstances.*" (Italics ours.) The amount of the respondent's *net income* was necessarily, under the statute, a basic factor in the comparison of respondent with representative corporations. The alteration of respondent's net income, by the allowance of additional deductions of $520,733.33 for 1918 and $104,571.43 for 1919, changed not only the "net income" but also the "profits per unit of business transacted," the "amount * * * of war profits or excess profits," and the relation between capital employed and net income." It is, obviously, impossible to know whether the Commissioner would have used the same or even similar comparatives had he known that the respondent's net income for 1918 and 1919 was very substantially less than he then found it to be. What "other relevant facts and circumstances" went into his selection of comparatives does not appear. Indeed, the record contains no data as to the Commissioner's selection of comparatives. It can not be known whether the Commissioner's ratios of tax to income were the proper ones to be applied to respondent's reduced net income. More-

[1] An excellent idea of the inter-relation of "net income" with the considerations upon which both the right to special assessment (under Section 327 (d)), and the computation of the tax are determined is obtained from the "Comparative Statistics Data Sheet," Treasury Department Form No. 7885, Appendix B, p. 60, *infra*, used in special assessment cases.

over, it may well be that a reexamination of comparatives in view of the changed factors would show that the tax as computed without the benefit of special assessment was not disproportionate to that of representative corporations and consequently no need for special assessment."

Neither the granting of a new special assessment on respondent's revised net income nor the recomputation of the taxes could be made until performance of the preliminary tasks required of the Commissioner. The ratio of tax to income may not be fixed arbitrarily. To specific terms Section 328 (b) provides that "In any case, the actual ratio when ascertained shall be used in determining the correct amount of the tax." If the tax is properly to be computed under Sections 327 and 328 it must be determined in the manner required by the statute. "When a statute limits a thing to be done in a particular mode, it includes the negative of any other mode." *Botany Worsted Mills v. United States*, 278 U. S. 282, 289. The method of computation so provided has been confided to the Commissioner and the Board of Tax Appeals, but denied to the courts. In the instant cases the court below made no attempt to perform the preliminary tasks required by the statute but arbitrarily adopted special assessment ratios used by the Commissioner under quite different circum-

[10] Cf. Appeal of *Chalmers Publishing Co.*, 1 B. T. A. 929, where such a result was reached on review by the Board.

stances. The Circuit Court of Appeals, therefore, determined new profits taxes by a method lying outside the scope of its authority [17] and, moreover, made its computations without performing the duties which under the statue are a prerequisite thereto.

A substantially similar situation was presented in *Cleveland Automobile Co.* v. *United States* (N. D. Ohio), decided February 24, 1932, *supra.* There, as here, the taxes were determined by special assessment. After the taxes had been so computed the taxpayer claimed that they were excessive by reason of overvaluation of inventory by the Commissioner. There, as here, the taxpayer brought suit in the District Court to recover taxes alleged to have been illegally assessed. Although the court reached the conclusion that the Commissioner's valuation of the inventory was proper, it definitely considered the question of its authority to review the Commissioner's determination of the profits taxes, and held that it had none. The court said:

> If the net income of the taxpayer may be reduced upon consideration by the Court, the tax as determined by the Commissioner will cease to bear the same ratio to the net income of the taxpayer as the average tax of

[17] In *Oak Worsted Mills* v. *United States*, 38 F. (2d) 699, 704 (C. Cls.), Judge Littleton said in his concurring opinion: "To go into the question whether the Commissioner had authority to change his determination and reassess a portion of the tax refunded under the special assessment provisions would be the same as inquiring into the correctness of such determination."

> representative corporations engaged in a like or similar trade or business bears to their average net income for the years in question. In other words, should the Court determine that the Commissioner erroneously adopted an illegal method for valuation of the plaintiff's inventory, requiring a reduction in net income, it would not be proper, in my judgment, to apply the rate computed by the Commissioner.
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> * * * * *
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> To do so, it seems to me, would result in opening up the entire subject of tax computation and require the Court to review every factual element entering into the special assessment.

The chief fallacy in the argument of the respondent and in the decision of the Circuit Court of Appeals lies, we think, in the assumption that the ultimate function of the Commissioner under Sections 327 and 328 is to determine for the particular taxpayer a *rate of tax,* which, once determined, must be used for that taxpayer despite radical changes in the factors which were used in determining the rate. There is nothing in the language of the statute or the court decisions interpreting it which supports this view.[18] On the contrary, the

[18] In this respect the determination of profits taxes by special assessment differs radically from the ordinary method, in which the statute specifies a *rate* which is uniformly applicable to net income. See Revenue Act of 1918, §§ 210 (a) and (b), 211 (a), 230 (a) (1) and (2), 301 (a) and (b).

language of the statute shows plainly that the object sought and the duty placed upon the Commissioner is the *determination* and *computation* of the *tax*. Section 327 provides:

> That in the following cases the *tax shall be determined* as provided in section 328.

In Section 328 it is provided that:

> In the cases specified in section 327 *the tax* shall be the amount * * *.

In the second paragraph of Section 328 it is provided that:

> In *computing the tax* under this section the Commissioner shall compare the taxpayer only with representative corporations. * * *.

Subsection (c) of Section 328 provides:

> The Commissioner shall keep a record of all cases in which *the tax is determined* in the manner prescribed in subdivision (a) * * *. (Italics ours.)

Moreover, in the *Williamsport case* the Court made no mention of the determination of a *rate* of tax, but referred repeatedly to the "computation" of the tax, which, the Court said, was vested in the Commissioner "in all cases." (See pp. 13–14, *supra*.)

Clearly, the problem before the court below was not "the simple mathematical operation of applying the Commissioner's rates to the true income," as asserted by the respondent in its brief in op-

position (pp. 2, 6, 7). The use of the ratio of tax to income in special assessment cases is but an incidental, though necessary, operation in the computation of the tax, which is the end sought by the statute. Once determined, the ratio is not a factor which remains constant for a particular corporation, notwithstanding variations in the underlying factors upon which its determination is based. On the contrary, it remains correct only so long as these factors are not changed in such a manner as would effect a change of the comparatives. The discretionary acts which are removed from judicial review consist in the determination of the existence of "abnormal conditions" or of "exceptional hardship" evidenced by "gross disproportion" between the tax computed in the normal way and that computed by special assessment, the selection of "representative corporations" similarly situated, the determination of their "net income" excess profits, and like matters. These tasks are all directed to one end—the computation *of the tax*. Once performed, the determination of the ratio is a mere mathematical computation, easily made and involving in itself no exercise of discretion.

The respondent is quite inconsistent in arguing in its brief in opposition that the court below might redetermine the profits tax *qua* tax, although, as it concedes, the court had no power to change the determined ratio. This argument overlooks

the obvious fact that by applying the Commissioner's special assessment ratio to a revised net income the court was necessarily revising the ratio. It was the failure of the court below to appreciate that the tax ratio found by the Commissioner was relevant in the computation of the tax only so long as the underlying factors remained unchanged, which we think led to the erroneous conclusion that they might compute anew respondent's profits taxes by employing the "rates" used by the Commissioner.

The respondent in its brief in opposition (pp. 10–11) concedes that the special assessment ratios applied by the Circuit Court of Appeals to the reduced net income were not the *correct* ratios, but since, as it asserts, the correct rates must necessarily have been lower than the rates used by the court, the Government suffered no harm. Putting to one side the requirement of the statute that "In any case, the actual ratio when ascertained shall be used in determining the correct amount of the tax," the respondent's argument is fallacious because, as above pointed out, it can not be known (1) whether in the light of the reduced income respondent still is entitled to special assessment and (2) if so, that the rate of the tax must necessarily be lower.

In its brief in opposition (pp. 4, 11, 12) the respondent emphasizes its offer to prove at the trial that the abnormality upon which its special assess-

ments were based was an abnormality of *capital* and not of *income*—"for the purpose of establishing that any change in income could not remove the abnormality." The import of this suggestion is that the respondent would continue to remain entitled to special assessment no matter what reduction the court might make in its net income. The mere statement of this argument would seem clearly to illustrate its lack of foundation, since it completely overlooks the necessary correlation between capital and income in all determinations of the applicability of Section 327 (d). The test of applicability is not merely whether "abnormal conditions affecting the capital or income" exist, but whether such conditions create a gross disproportion between the tax computed in the normal manner and the average tax of representative corporations. Obviously, any substantial change in the net income, whether or not the capital remains unchanged, affects the applicability of Section 327 (d).

In its brief in opposition (pp. 10–11) the respondent argued that the statutory profits-tax rate is a graduated rate, that whenever the net income is decreased the tax rate also decreases, that since its net income was reduced its profits-tax rate should also have been reduced, but that since the *rate* can not be changed by the courts, the least the court below could do was to apply the erroneous, because too high, rates used by the Commissioner, and

this give the respondent at least a portion of the relief to which it was entitled. We think that what has been said above shows this argument also to be unfounded. It is true that when profits taxes are computed in the normal manner the tax rates are graduated as the statute requires; but when the taxes are computed by special assessment there is no "rate" other than the ratio of tax to net income of the comparatives selected. (Pp. 21–23, *supra*.) In Appendix C (p. 41, *infra*) we have set forth a computation showing how it might well happen that, by reason of the selection of comparatives having a higher ratio of tax, a taxpayer's profits tax would not necessarily be diminished by reason of a decrease in its net income.[19]

If the courts may in such a case as this redetermine profits taxes their power is necessarily limited to a redetermination of such taxes without special assessment, i. e., under Section 301 of the

[19] In the court below the respondent charged that a somewhat similar suggested computation was improper because it dealt with exaggerated and wholly supposititious circumstances. But it must be remembered that the special assessment provisions of the statute are applicable only in unusual cases, and if the relation of capital to income, as set out in the illustrated case (p. 41, *infra*), had been normal, special assessment would not have been allowed. Viewed in this light we think the suggested computation fairly reflects a possible situation and computation under the statute

statute.[20] Determination of profits taxes in the normal manner, under Section 301, involves the exercise of no discretionary administrative duties and represents the limit to which a court may go without invading the field left to the discretion of the Commissioner.

Congress may not have intended that a taxpayer should be compelled to pay a profits tax under Sections 327 and 328 in excess of that due under Section 301. But if a court, although without power to compute a taxpayer's profits taxes *by special assessment* as attempted in the instant cases, possesses the power to set aside the Commissioner's determination to the extent of reducing the tax to the amount due at normal excess profits rates without special assessment, there is no room or necessity for the operation of even this limited jurisdiction in the cases at bar. Although the Circuit Court of Appeals did not attempt to determine the amounts of profits taxes which would be payable by respondent on its reduced net income at normal excess profits rates, the respondent conceded in the court below that such taxes would be greater in

upon a reduction in net income. The Commissioner is required by the statute to select representative corporations. If such representative corporations show a higher tax ratio than that of corporations which would be representative if the taxpayer's net income were greater, it would not justify the Commissioner in refusing to apply the applicable ratio.

[20] Cf. the concurring opinion of Judge Littleton in *Oak Worsted Mills* v. *United States*, 38 F. (2d) 699, 704 (C. Cls.).

amount than the profits taxes as computed by the Commissioner.[21]

CONCLUSION

Whether the lack of judicial power to redetermine respondent's profits taxes will result in its being required to pay a larger amount of tax than it should pay is wholly problematical, and cannot be determined without the performance anew of the statutory functions of the Commissioner. Such functions are beyond the province of a court, and no provision is found in the statute whereby the instant cases may be referred to the Commissioner for redetermination of the profits taxes in light of the reduced net income. Assuming that this situation results in hardship to the respondent, the responsibility, if any, must be ascribed to the

[21] The Bureau of Internal Revenue has made a computation of the profits taxes which would be due from respondent under Section 301 upon the net income and invested capital as revised by the allowance of additional deductions in the Circuit Court of Appeals. This computation indicates that the profits taxes as so computed would be greater by $113,309.24 for 1918 and by $203,793.23 for 1919 than the taxes as computed by the Commissioner under special assessment. Attention is called to the fact that these figures are slightly different than the figures appearing in the computation referred to in footnote 4, page 11, of the petition for certiorari. We are advised by the Bureau that this earlier computation contained certain slight inaccuracies, and that as to each year it reflected the difference between the total taxes paid (income and profits taxes) and the amount of the income and profits taxes as then computed under section 301 upon the revised net income.

statute itself and respondent's choice to proceed under it. General principles of law should not be sacrificed in order to obtain what the court conceives to be justice in a particular case. The effect of a decision upon a particular taxpayer is an unsafe guide in determining legal principles of the kind here involved.

We submit that the judgment of the Circuit Court of Appeals, so far as it affects the Commissioner's determination of respondent's profits taxes, should be reversed.

Respectfully submitted.

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FEBRUARY, 1933.

APPENDIX A

STATUTES AND REGULATIONS

Revenue Act of 1918, c. 18, 40 Stat. 1057, 1093:

SEC. 327. That in the following cases the tax shall be determined as provided in section 328:

(a) Where the Commissioner is unable to determine the invested capital as provided in section 326;

(b) In the case of a foreign corporation;

(c) Where a mixed aggregate of tangible property and intangible property has been paid in for stock or for stock and bonds and the Commissioner is unable satisfactorily to determine the respective values of the several classes of property at the time of payment, or to distinguish the classes of property paid in for stock and for bonds, respectively;

(d) Where upon application by the corporation the Commissioner finds and so declares of record that the tax if determined without benefit of this section would, owing to abnormal conditions affecting the capital or income of the corporation, work upon the corporation an exceptional hardship evidenced by gross disproportion between the tax computed without benefit of this section and the tax computed by reference to the representative corporations specified in section 328. This subdivision shall not apply to any case (1) in which the tax (computed without benefit of this section) is high merely because the corporation earned within the taxable year a high rate of profit

upon a normal invested capital, nor (2) in which 50 per centum or more of the gross income of the corporation for the taxable year (computed under section 233 of Title II) consists of gains, profits, commissions, or other income, derived on a cost-plus basis from a Government contract or contracts made between April 6, 1917, and November 11, 1918, both dates inclusive.

SEC. 328. (a) In the cases specified in section 327 the tax shall be the amount which bears the same ratio to the net income of the taxpayer (in excess of the specific exemption of $3,000) for the taxable year, as the average tax of representative corporations engaged in a like or similar trade or business, bears to their average net income (in excess of the specific exemption of $3,000) for such year. In the case of a foreign corporation the tax shall be computed without deducting the specific exemption of $3,000 either for the taxpayer or the representative corporations.

In computing the tax under this section the Commissioner shall compare the taxpayer only with representative corporations whose invested capital can be satisfactorily determined under section 326 and which are, as nearly as may be, similarly circumstanced with respect to gross income, net income, profits per unit of business transacted and capital employed, the amount and rate of war profits or excess profits, and all other relevant facts and circumstances.

(b) For the purposes of subdivision (a) the ratios between the average tax and the average net income of representative corporations shall be determined by the Commissioner in accordance with regulations pre-

scribed by him with the approval of the Secretary.

* * * * *

In any case, the actual ratio when ascertained shall be used in determining the correct amount of the tax. * * *

(c) The Commissioner shall keep a record of all cases in which the tax is determined in the manner prescribed in subdivision (a), containing the name and address of each taxpayer, the business in which engaged, the amount of invested capital and net income shown by the return, and the amount of invested capital as determined under such subdivision. The Commissioner shall furnish a copy of such record and other detailed information with respect to such cases when required by resolution of either House of Congress, without regard to the restrictions contained in section 257.

Regulations 45 (1920 Edition), issued under the Revenue Act of 1918:

ART. 901. *Treatment of special cases.*—In the cases specified in section 327 of the statute the tax will be specially determined under the provisions of section 328, but the tax will not ordinarily be computed under section 328 merely because the corporation's form or manner of organization, or the limitations imposed by section 326, result in a greater tax than would otherwise be payable. A corporation which comes within the provisions of subdivision (d) of section 327 may make application for assessment under the provisions of section 328, which application shall be attached to its return in the form of a statement seting forth in full: (a) the reasons why the tax should be so determined;

(b) the facts upon which such reasons are based; (c) an exact description of each trade or business or important branch of a trade or business carried on by it; (d) a statement of the invested capital and net income for each year since the beginning of the prewar period; and (e) a statement showing the amount of gains, profits, commissions, or other income derived on a cost-plus basis from Government contracts made after April 5, 1917, and before November 12, 1918, and showing the per cent which such income is of the total income of the corporation. See sections 1 and 326 and articles 831–871 and 1510.

ART. 911. *Computation of tax in special cases.*—In the cases specified in section 327 of the statute the tax is to be computed by comparison with representative corporations whose invested capital can be satisfactorily determined under section 326 and which are engaged in a like or similar trade or business and similarly circumstanced. The provisions of section 328 do not permit the determination of a general average for any trade or business. In each case which comes under the provisions of section 327 the Commissioner will determine, as nearly as may be, the group or class of corporations with which the corporation should be compared and the amount which bears the same ratio to the net income of the corporation (in excess of the specific exemption of $3,000) for the taxable year as the average tax of such representative corporations bears to their average net income (in excess of the specific exemption of $3,000) for such year. The comparison will take account of similarity with respect to gross income, net income, profit per unit of business transacted, and

capital employed, the amount and rate of war profits or excess profits, and all other relevant facts and circumstances.

RULE 62.—SPECIAL ASSESSMENT

(*a*) If some of the issues raised by the petition involve section 327 or section 328 of the Revenue Act of 1918 or of 1921 [or section 210 of the Revenue Act of 1917, as the case may be], and some do not involve such sections, the hearing may, in the discretion of the Board, on motion, be limited in the first instance to trial of the issues which do not involve such sections.

(*b*) A hearing may, in the discretion of the Board, on motion, be had, limited to the trial of the issue whether the petitioner is entitled to have its tax determined as provided in section 328 [or section 210, as the case may be].

(*c*) If the Board decides that the petitioner is entitled to have its tax determined as provided in section 328 [or section 210, as the case may be], the respondent shall within 60 days after such decision file with the Board an original and two copies of a proposed redetermination showing the method of the computation. If, within 20 days after service by the Board upon the petitioner of a copy of such proposed redetermination, the parties are unable to agree upon the amount of tax, either party may move, or the Board may upon its own motion order, that the case be placed upon the day calendar for further hearing, at which either party may submit proof of the correct amount of tax and deficiency or overpayment.

(*d*) If from the pleadings or otherwise it appears of record before the Board that the parties agree that petitioner is entitled to have its tax determined as provided in section 328 [or section 210, as the case may be], and the only issue is as to the correct amount of the tax so determined, the case will be placed upon the day calendar in due course for hearing, at which either party may submit proof of the correct amount of the tax and deficiency or overpayment.

APPENDIX B

Income tax, audit review, special assessment

[Comparative statistics data sheet—Special cases—19..]

Comparative statistics re:.....Nature of business.....Case No.....

	Appellant	Comparative No. 1	Comparative No. 2	Comparative No. 3	Comparative No. 4	Comparative No. 5	Comparative No. 6	Average comparatives
Location								
Date of organization								
1. Invested capital as adjusted								
2. Statutory intangibles								
3. Adjustments for inadmissible assets								
4. Interest-bearing indebtedness								
5. Noninterest-bearing indebtedness to stockholders								
6. Gross sales								
7. Other income								
8. Cost of goods sold								
9. Ordinary and necessary expenses								
10. Compensation of officers								
11. Repairs								
12. Interest								
13. Taxes								
14. Bad debts								
15. Exhaustion, wear and tear (including obsolescence)								
16. Amortization of war facilities								
17. Depletion								
18. Special deductions from income								
19. Net income								
20. Percentage of net income to gross sales								
21. Percentage of net income to adjusted invested capital								
22. Percentage of cost of sales to gross sales								
23. Excess profits credit								
24. War profits credit								
25. Net income per unit of business								
26. Profits tax								
27. Percentage of profits tax to net income								
28. Net income previous year								
29. Average net income prewar period								
30. Average invested capital prewar period								
31. Percentage of net income to invested capital prewar period								

NOTE.—Enter on the data sheet for both the appellant and the comparatives only statutory figures.

Prepared by ..... Resident auditor.
Checked by ..... Date, ...
Reviewed by ..... Section auditor.

Final profits tax..... Appellant . $.....
Per cent of final tax to net income..... Appellant $.....
Constructed invested capital..... Appellant . $.....

APPENDIX C

Taxpayer company:	
Invested capital	$100,000
Net income	100,000
Statutory tax computed under Section 302	69,100
Comparatives before reduction in net income:	
Average invested capital	300,000
Average net income	100,000
Average statutory tax computed under Section 301	53,600

Tax on basis of the above comparatives is 53.6% of the net income.

If a reduction in net income of $17,000 be allowed then the situation is as follows:

Taxpayer company:	
Invested capital	$100,000
Net income	83,000
Statutory tax computed under Section 302	55,500

Upon a reexamination of the comparatives the Commissioner might find the following situation with respect thereto:

Comparatives after reduction of net income:	
Average invested capital	$120,000
Average net income	83,000
Average statutory tax computed under Section 301	54,400

Tax on the basis of the above comparatives is 65.5% of the net income.

In view of this situation it is entirely probable that the taxpayer would still be entitled to a special assessment, but that notwithstanding the decrease in income of $17,000 the tax computed on the basis of the new comparatives is greater than the tax computed on the basis of the former comparatives and prior to the reduction in income. The taxpayer thus would be liable for an additional tax notwithstanding the decrease in net income, both computations being made under Section 328.

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IN THE

Supreme Court of the United States,

OCTOBER TERM—1932.

Nos. 476, 477, 478.

D. B. HEINER, Collector of Internal Revenue for the 23rd District of Pennsylvania,

Petitioner,

vs.

DIAMOND ALKALI COMPANY, a corporation.

C. G. LEWELLYN, formerly Collector of Internal Revenue for the 23rd District of Pennsylvania,

Petitioner,

vs.

DIAMOND ALKALI COMPANY, a corporation.

BRIEF OF DIAMOND ALKALI COMPANY IN OPPOSITION TO PETITION FOR WRITS OF CERTIORARI.

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IN THE

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Nos. 476, 477, 478.

D. B. HEINER, Collector of Internal Revenue for the 23rd District of Pennsylvania,
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vs.

DIAMOND ALKALI COMPANY, a corporation.

C. G. LEWELLYN, formerly Collector of Internal Revenue for the 23rd District of Pennsylvania,
Petitioner,

vs.

DIAMOND ALKALI COMPANY, a corporation.

BRIEF OF DIAMOND ALKALI COMPANY IN OPPOSITION TO PETITION FOR WRITS OF CERTIORARI.

The Solicitor General heretofore filed in this court a petition for writs of certiorari to the Circuit Court of Appeals for the Third Circuit to review the judgments of that court entered on July 26, 1932 (R. 181, 187, 193, Nos. 4419 & 4426; R. 124, 130, 135, No. 4427). One judgment was entered in the *Lewellyn* case which related to the taxable year 1919.

Two judgments, identical in terms, were entered in the *Heiner* case, disposing of the cross appeal of Collector Heiner and the appeal of the taxpayer.

Opinions Below.

The opinion of the District Court disposing of both cases is recorded in 39 Fed. (2nd) 645. Both the original opinion and the opinion upon reargument of the Circuit Court of Appeals are reported in 60 Fed. (2nd) 505 (R. 169, 188, Nos. 4419 & 4426; R. 112, 131, No. 4427).

Jurisdiction.

The jurisdiction of this court is invoked under Section 240(a) of the Judicial Code (43 Stat. 938; 28 U. S. C. A. Sec. 347).

Question Presented.

The petition for writs of certiorari does not accurately state the question presented. Such question may be more accurately stated as follows: Whether the Court's disability to review or change excess profits tax rates as found by the Commissioner under Section 328 (special assessment) shall be extended so as to prohibit the Court from correcting errors in income made by the Commissioner and from performing the simple mathematical operation of applying the Commissioner's rates to the true income.

Statutes Involved.

The statutes involved are Sections 327 and 328 of the Revenue Act of 1918 (c. 18, 40 Stat. 1057, 1093). Section 328 is set out in full at page 13 of the petition and Section 327 is set out in part on the same page. The whole of Section 327 is pertinent and it is as follows:

"SEC. 327. That in the following cases the tax shall be determined as provided in section 328:

"(a) Where the Commissioner is unable to determine the invested capital as provided in section 326;

"(b) In the case of a foreign corporation;

"(c) Where a mixed aggregate of tangible property and intangible property has been paid in for stock or for stock and bonds and the Commissioner is unable satisfactorily to determine the respective values of the several classes of property at the time of payment, or to distinguish the classes of property paid in for stock and for bonds, respectively;

"(d) Where upon application by the corporation the Commissioner finds and so declares of record that the tax if determined without benefit of this section would, owing to abnormal conditions affecting the capital or income of the corporation, work upon the corporation an exceptional hardship evidenced by gross disproportion between the tax computed without benefit of this section and the tax computed by reference to the representative corporations specified in section 328. This subdivision shall not apply to any case (1) in which the tax (computed without benefit of this section) is high merely because the corporation earned within the taxable year a high rate of profit upon a normal invested capital, nor (2) in which 50 per centum or more of the gross income of the corporation for the taxable year (computed under section 233 of Title II) consists of gains, profits, commissions, or other income, derived on a cost-plus basis from a Government contract or contracts made between April 6, 1917, and November 11, 1918, both dates inclusive."

Statement.

The taxpayer duly filed income and profits tax returns for the calendar years 1918 and 1919. On the face of the return filed for 1918 claim was made that its profits taxes should be computed under Sections 327 and 328 of the Revenue Act of 1918 (Ex. LL, B. E. Vol. II, p. 635). Thereafter

a similar claim was made with respect to the year 1919. The Commissioner determined that owing to abnormal conditions the profits taxes, if determined in the ordinary way, would work an exceptional hardship upon the taxpayer evidenced by gross disproportion between the tax as computed in the ordinary way and the tax as computed by special assessment. The taxpayer offered to prove at the trial that the abnormality upon which special assessment was conditioned was an abnormality of capital and not of income for the purpose of establishing that any change in income could not remove the abnormality. On objection by the petitioners this evidence was rejected (B. E. Vol. 1, p. 222).

The Commissioner found that the ratio of tax to income (tax rate) should be 54.54% for 1918 and 18.31% for 1919, arriving at such rates by taking the average rates of representative corporations.

The Commissioner made large income adjustments, determined deficiencies, assessed and collected the same, and in due course rejected the taxpayer's claims for refund. The taxpayer brought suits in the District Court for the Western District of Pennsylvania which court increased the deduction allowed by the Commissioner for amortization of war facilities but denied the other claims made by the taxpayer. The District Court applied the profits tax rates found by the Commissioner to the income as corrected by it.

On appeal the Circuit Court of Appeals increased the deduction for amortization of war facilities, but in its original opinion held that, notwithstanding the reduction of income, the profits taxes as found by the Commissioner should not be reduced. On rehearing the Circuit Court of Appeals found that the taxpayer was entitled to an additional deduction for depreciation in 1918 and that the profits tax rates as found by the Commissioner should be applied to the corrected net income in order to determine the correct profits tax liability of the taxpayer for each year in question.

The petitioners now ask this Court to review the final decision of the Circuit Court of Appeals and to hold that,

notwithstanding substantial reductions in income (more than $500,000 for 1918 and more than $100,000 for 1919), the profits taxes found by the Commissioner should nevertheless remain the same.

ARGUMENT.

POINT I.

The decision of the Circuit Court of Appeals does not conflict with principles announced by this Court or by other Circuit Courts.

The primary reason advanced by the petitioners for granting writs is that the decision below conflicts with the decision of this Court in *Williamsport Wire Rope Co.* v. *United States*, 277 U. S. 551.

In that case the sole question presented was whether or not the Court of Claims could review the Commissioner's determination that the taxpayer did not present a special case requiring that its profits tax rate be determined by reference to representative corporations. In its opinion this Court pointed out that the question presents such a complex and delicate phase of revenue administration that review by a large number of courts would tend to defeat rather than promote equality of application of the relief provisions, because the courts would not have ready access to the necessary, voluminous data and because their experience in passing upon questions of that kind is limited. The decision emphasizes the necessities and practicalities of the situation rather than jurisdiction. As a practical matter the courts would be unable to determine whether the Commissioner erred in his selection of comparatives or representative corporations unless they had unlimited access to the files of the Commissioner. It would be impossible for trial courts to obtain all this data and impracticable to consider

it even if it were obtainable. It is true the delegation of this work to the Commissioner removes it from the hands of the courts, but they are not thereby deprived of jurisdiction to correct other errors in the case of any taxpayer whose profits tax rates have been determined from representative corporations. While the question before the Court was the right to special assessment, the decision clearly applied also to the equally delicate and complex matter of ascertaining the tax rate from representative corporations, and this Court has declined to review that question in the absence of irregularity. *Brown's "Shamrock" Linens, Ltd.* v. *Bowers*, 48 Fed. (2nd) 103 (C. C. A. 2nd), cert. denied, 283 U. S. 865.

Once the delicate and complex questions of whether special assessment should be granted and, if so, what the rate should be are decided as an administrative matter, certainly nothing delicate or complex is left in multiplying such rate by the correct net income and nothing that this Court has said and no principle that this or any other Court has announced can be so construed.

Since the decision in the *Williamsport Wire Rope* case many cases have come before the courts either on original jurisdiction or by appeal from the Board. Most of them involved either the denial of special assessment or the propriety of the rate found by the Commissioner. *Brown's "Shamrock" Linens, Ltd.*, v. *Bowers*, 48 Fed. (2nd) 103 (C. C. A. 2nd), cert. denied 283 U. S. 865, was a case of a foreign corporation which did not complain of the income found by the Commissioner but was solely concerned with the rate. *Standard Rice Co.* v. *Commissioner*, 41 Fed. (2nd) 481 (C. C. A. 5th), held that where the Board sustained the Commissioner's denial of special assessment the Court would not review on an appeal from the Board. *Oak Worsted Mills* v. *United States*, 38 Fed. (2nd) 699 (Ct. Cls.), merely held the obvious, namely, that the Commissioner could, within the statutory period of limitation, revise his computation of the tax under special assessment. Other cases

cited in the petition were confined entirely to the questions of denial of special assessment, the propriety of the rate, or whether or not the Commissioner had acted in a manner so arbitrary as to constitute abuse of discretion. None went any further. None purported to decide or even to imply that there is discretion in the simple act of multiplying an income by a rate.

The question here involved was not present in any of the cases that have been decided either by this Court or the Circuit Courts of Appeals.

The question was considered but not decided in one District Court case, *Cleveland Automobile Company* v. *United States* (Feb. 24, 1932, N. D. Ohio, not yet reported). That case was one in which the taxpayer contended that the Commissioner had improperly valued its inventory and thereby overstated its income. The Government defended on the grounds that the inventory had been correctly determined by the Commissioner and that in any event income could not be revised by the Court because the profits tax had been determined by special assessment. While the Court expressed doubt as to whether it could change the income it finally concluded that on the merits there was no error in the Commissioner's determination of income. This finding as to the correctness of the income was necessary to any decision of the case because even if the Court had believed it could not change the income for profits tax purposes it unquestionably must have known that it had jurisdiction to change the income for income tax purposes since the income taxes are never a matter of special assessment. Therefore, all that the court said regarding its jurisdiction over the profits tax became dictum. We are impelled, however, to go further and point out that the court did not have before it the full significance of the matter for, in the course of its opinion, it suggested that the income must have been correct for purposes of the profits tax under special assessment since the taxpayer, an automobile dealer, was no doubt compared with other automobile dealers who must have had the same inventory problems and whose income,

therefore, presented the same problem as the taxpayer's. This is an obvious misconception because income is not determined from representative corporations. It is required to be determined on the merits and only the average ratio or rate of profits taxes paid by representative corporations is employed in determining the profits tax of a taxpayer under special assessment. Therefore it is apparent that both on its reasoning and because its discussion of the instant question was dictum the decision of the District Court does not conflict with the decision in the cases at bar.

Accordingly it is submitted that the petitioners' primary ground, namely, conflict between the decision below and other decisions, is without merit.

POINT II.

The decision of the Circuit Court of Appeals is not erroneous; on the contrary it is correct and judgments for any less would be unconscionable.

In opposition to the second ground presented in the petition we assert that the correctness and justice of the decision is clearly demonstrable and further that petitioners' claim is unjust, resulting in a delegation of power to the Commissioner that can not be presumed in the absence of clear and compelling statutory language. Their position leads to startling results when examined.

Petitioners contend that the profits taxes found by the Commissioner must not be disturbed even though income is reduced. In the exercise of his discretionary power he found the rate for 1918 at 54.54% and applying this to his concept of the net income found a profits tax for that year of $2,084,324.26. The Court below reduced the net income of $3,821,134.63 found by the Commissioner by $529,733.33 or to

the correct net income of $3,291,401.30. The Commissioner's profits tax is not 54.54% of the correct net income, *but is more than 63% thereof.* With different figures the result in 1919 is similar. If the profits tax must be left undisturbed the effect is either: (1) the courts do not have jurisdiction to correct any errors of income once a profits tax has been computed by special assessment; or, (2) the courts in order to sustain the Commissioner's assessment must apply a higher rate of profits tax whenever income is reduced to the correct amount.

Denial to taxpayers of the right to have a court review the Commissioner's determination of income wherever the Commissioner computed the profits tax rate by special assessment would be far reaching. Profits tax rates must be determined from representative corporations in the case of (1) all foreign corporations, (2) all corporations whose invested capital cannot be determined, (3) all corporations whose capital paid in consisted of tangible and intangible property not clearly severable, and (4) all corporations which had an abnormality of capital or income, or both, that resulted in a gross disproportion in their profits tax rate computed in the ordinary way when compared with the profits tax rates of representative corporations (See Section 327, *ante*). The claim of the petitioners in essence is that in all classes of cases enumerated above the Commissioner is intended to be the sole and final judge of what constitutes income under the Sixteenth Amendment, how much the income is in any case, and what deductions taxpayers are entitled to take. It would confer upon the Commissioner the authority to decide constitutional questions without review and to tax that which is constitutionally not income, such as stock dividends from foreign corporations received by domestic corporations, stock rights similarly received, proceeds of life insurance upon an officer of a corporation and the like. Compare *Eisner* v. *Macomber*, 252 U. S. 189; *Miles* v. *Safe Deposit & Trust Co.*, 259 U. S. 247; *U. S.* v. *Supplee-Biddle Hardware Company*, 265 U. S. 189. Carried to its logical conclusion the petitioners' con-

reduce it. Therefore, when the court fixed the profits tax by the simple process of multiplication at 75% of the corrected net income of 1919, for example, it merely gave the taxpayer so much of the relief to which it was entitled as the court was empowered to give.

The petitioners argued below that the changing of the income might produce a situation where the computations used for the lower income would not be correct. However, this reduction in income, which would carry with it a reduction in the profits per unit of business mentioned in the statute, would not result in a change in capital or a change in the nature of the business, or in any other important factor incident to the selection of comparatives. Only two factors, income and capital, can affect the profits tax rate. In this case there was no change of capital. Therefore, comparatives selected to reflect the situation of a reduced income must show a lower rate than that shown by proper comparatives selected to fit the situation of a greater income. And this would be true in all cases involving this question.

This taxpayer brought its suits in the District Court before it was decided that a review of special assessment rates fixed by the Commissioner was withheld from the Courts by Congress. Having suffered that misfortune it is now forced to accept the rate of 75% for 1918 and 1919, for 1919 instead of having the right to reduce rates to accord with the reduced income. Accordingly, it does not lie in the mouths of the petitioners to assert that the judgments of the court below are erroneous. The judgments apply assessable profits tax rates to corrected income. The result is just and fair so far as the Court's power to review permits. To deprive it of the power of reaching this result would be unconscionable.

In a footnote on page 11 of the petition it is stated that a computation by the Bureau of Internal Revenue shows that profits taxes computed under Section 301, that is, without special assessment, would be more on the basis of the re-

duced income than the profits taxes paid by the taxpayer. This statement off the record is apparently made in order to suggest to the Court that it should now reverse the Commissioner's allowance of special assessment and recompute the tax under Section 301 in order to decide whether or not the taxpayer is entitled to a refund. The clear answer to this suggestion, however, is that where any of the conditions set forth in Section 327 exist the profits tax rate *must* be computed under Section 328 since the provisions of that section are not permissive but mandatory. It has already been pointed out that the abnormality in these cases is one of capital and the only change made by the court is in income. The abnormality, one of the conditions of special assessment, therefore remains. The figures in the footnote, if correct, serve to show that the tax computed under Section 301 would be grossly disproportionate to the tax computed under Section 328, even using the unreviewable rates which on reason are too high. Such figures thus establish the other condition of special assessment under Section 327 (d), namely, a gross disproportion between the taxes computed by the two methods.

On the same page of the petition it is stated that the Commissioner gives taxpayers opportunity to withdraw the request for special assessment if they are not satisfied with the income found by him, citing *Chalmers Publishing Co.* v. *Commissioner*, 1 B. T. A. 629. That case does not in any conceivable sense support the assertion. Since special assessment is mandatory if the conditions set forth in Section 327 exist, it would be impossible for the Commissioner validly to give any such right to taxpayers. Subsections (a), (b) and (c) of Section 327 require the use of Section 328 in any event. Subsection (d) requires such use when the abnormality and the gross disproportion are found. We, therefore, challenge the existence of any such custom and deny that it could be proper under the statute.

Under the *Williamsport* decision neither the Commissioner's refusal to grant special assessment nor the profits tax

rate found by him if he has granted special assessment is subject to court review provided the Commissioner has properly exercised his discretionary power. But the petitioners now seek a decision by this Court that, special assessment having been granted and a rate determined, plain errors in income may not be reviewed or corrected by the courts. The ascertainment of the correct net income under the law embraces matters of fact and law which are not limited by administrative discretion. Certainly taxpayers of this country are not to be deprived of all judicial review and remedy when their money has been exacted on the basis of mistakes of an administrative bureau in ascertaining facts or construing statutes. A direct attempt by Congress to do such a thing would be shocking. This attempt to read such an intent into purely relief provisions of the statute is even more shocking.

POINT III.

The question involved is not an important one.

The petition, for its third ground, states that this question is presented in pending cases involving some $2,000,000. Apparently that amount does not turn on this question alone, but is the amount involved in pending cases in which this question among others may be presented. In any event, this question, involving as it does only the war tax years, would seem to be of very narrow present or future application. It must soon be a dead issue. In fact it was never a live issue before these cases in which it was raised by the Government for the first time. No useful purpose can now be served by granting the petitioners an opportunity to ask that this Court extend the *Williamsport Wire Rope* decision so as to produce a demonstrably unjust and unconscionable result.

Under the third ground it is also suggested in vague, general terms that this question bears upon the Commissioner's discretionary powers under later Revenue Acts. No spe-

cific reference is made to the powers or the Acts conferring them. A careful scrutiny of all the later acts does not disclose any grant of administrative discretion which could be affected even remotely by the decision below or by a decision of this court.

CONCLUSION.

It is respectfully submitted that these cases do not warrant a review by this Court.

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BRIEF FOR DIAMOND ALKALI COMPANY.

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OCTOBER TERM—1932.

Nos. 476, 477 and 478.

D. B. HEINER, Collector of Internal Revenue for the 23rd District of Pennsylvania,

Petitioner,

against

DIAMOND ALKALI COMPANY, a corporation,

Respondent,

C. G. LEWELLYN, formerly Collector of Internal Revenue for the 23rd District of Pennsylvania,

Petitioner,

against

DIAMOND ALKALI COMPANY, a corporation,

Respondent,

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

BRIEF FOR DIAMOND ALKALI COMPANY

Opinions of the Courts Below.

The opinions of the Circuit Court of Appeals for the Third Circuit, both on the original and the rehearing, are reported

in 60 Fed. (2nd) 505. The findings of fact and conclusions of law of the District Court in Nos. 476 and 477 relating to the year 1918 (R. 81) are reported in 39 Fed. (2nd) 645, but the findings and opinion in No. 478, relating to the year 1919 (R. 27), are not reported.

Statement of the Case.

The 1918 and 1919 income and profits tax returns of respondent were filed in due course. Respondent applied for computation of its profits taxes under Sections 327 and 328. Owing to an abnormality of capital (R. 55, Nos. 476, 477) the Commissioner determined that the profits taxes computed under Section 301 would work a hardship upon the respondent because such taxes would be grossly disproportionate to the taxes computed by reference to the representative corporations as provided by Section 328. He therefore computed the profits taxes by determining that ratio of respondent's net income for each year as the average profits tax of representative corporations bore to their net average income. The ratios so determined by the Commissioner were 54.54% for 1918 and 18.31% for 1919.

Following the filing of the returns, examinations and audits were made by the Commissioner and large additional taxes were from time to time proposed (R. 60, 69, 70, 75, Nos. 476 and 477), and sundry protests were filed and conferences held (R. 70). Respondent's claims with respect to the various deductions, particularly amortization of war facilities and depreciation, were not allowed and the Commissioner's final determination of net income was $3,821,143.63 for 1918 and $2,708,248.07 for 1919. Using the ratios as determined by him under Section 328 he arrived at profits taxes of $2,084,324.26 for 1918 and $495,871.87 for 1919.

The taxes were paid, claims for refund filed, such claims rejected, and suit brought to recover back the additional taxes paid. In the claims for refund and the suits as filed the respondent contended that the profits tax rates employed by the Commissioner did not satisfy the statute because the taxpayer was not compared with representative corporations and that net income as computed by the Commissioner was greatly in excess of the true net income because he did not allow adequate deductions on account of depreciation and amortization of war facilities.

By agreement of counsel the point as to selection of comparatives and determination of profits tax rates was presented and argued prior to the trial. The trial court held, adversely to the respondent and in favor of the petitioners, that it had no authority to review the administrative action of the Commissioner in selecting the comparatives to be used. Thereafter trial was had and the District Court found errors in the income as determined by the Commissioner, correcting it downward. Both parties appealed and the Circuit Court of Appeals further corrected the income downward. The case comes before this court with the correct income for 1918 standing at $3,291,410.30 instead of $3,821,143.63 as found by the Commissioner, and for 1919 at $2,603,676.64 instead of $2,708,248.07 as found by the Commissioner. Neither the District Court nor the Circuit Court of Appeals, in its second decision, disturbed the comparatives used by the Commissioner in arriving at the tax ratios found by him. The courts below merely applied the rates found by the Commissioner to the income as corrected by them. Both parties accept the income as now judicially determined to be the correct income.

The petitioners contend that since special assessment was applied for and granted the excess profits taxes as computed by the Commissioner must remain unchanged notwithstanding the fact that such taxes were the result of applying the unreviewable rates to incorrect income.

This state of facts and the issue drawn presents the following question.

Question Presented.

Whether the fact that the Commissioner determined the profits tax rates under Section 328 deprives the courts of power to correct mistakes in the amount of such taxes caused by admitted error in the Commissioner's determination of the amount of net income to which he applied his rates.

Statutes Involved.

The statutes involved are Sections 301(a), 327 and 328 of the Revenue Act of 1918 (c. 18, 40 Stat. 1058, 1088, 1093), which are printed in Appendix A, *infra*, pp. 22-24).

Summary of Argument.

I.

The Federal profits tax rates or ratios, however determined, must be applied to the correct net income. Where the income determined by the Commissioner is incorrect it must follow that the profits tax determined by him is incorrect.

The discretionary acts confided to the Commissioner by Sections 327(d) and 328 of the Revenue Act of 1918 do not

include an unreviewable determination of net income by him. When the court below judicially determined the true net income of respondent for 1918 and 1919 and applied the unreviewable rates or ratios determined by the Commissioner under Section 328 it neither reviewed nor set aside any discretionary act of the Commissioner. Its action was confined to matters of law and fact. Neither the decision of this court in *Williamsport Wire Rope Co.* v. *United States, infra,* nor any of the decisions denying review by the courts of the Commissioner's discretionary acts under Sections 327 and 328 have held to the contrary.

II.

Since it is self evident that the profits taxes must be based upon correct income and the Commissioner's ratios or rates determined under Section 328 are not reviewable, the court below was required to apply such ratios to the net income determined by it.

The Government suggests that if the Commissioner had determined net income at the same figures as the court determined it he might have used different comparatives and therefore different rates. "Might" does not mean "would". If the net income corrections were sufficiently substantial to have caused the Commissioner to use different comparatives and different rates the burden was upon the Government to prove it. The presumption is that the comparatives and the rates used by the Commissioner were correct.

Even assuming the use of different comparatives and different rates the result would be profits taxes lower than those found by the court. The profits tax (whether computed by rates taken directly from Section 301 or by the

average of rates of representative corporations whose profits tax rates were taken directly from Section 301) is computed from graduated rates. That is, when income increases the rates increase and when income decreases the rates decrease, and there is no such thing as a higher rate for a reduced income in any given case. If, therefore, it be assumed for the same of argument that different comparatives and different rates would have been used, in view of the lower incomes, such rates would have been lower than the rates that the Commissioner determined and the courts below applied. Hence the judgment is not prejudicial to the Government.

Petitioners' arguments all lead to the proposition that wherever the profits tax rate is determined under Section 328 errors of income that have been made by the Commissioner and the consequent errors in profits tax may not be corrected judicially. That proposition is unsound and unjust.

ARGUMENT.

I.

The action of the courts below was confined to matters of law and fact. No discretionary act of the Commissioner was either reviewed or set aside.

At the outset it should be pointed out that petitioners' statement of the question involved and their arguments are premised upon assumptions that are essentially erroneous. It is asserted that the court below set aside the special

assessment[1] made by the Commissioner and made a special assessment[1] of its own. This statement is not correct. It assumes everything to be argued in this case.

Section 328, under which the tax in special assessment cases is computed, provides in subsection (a) that the tax "shall be the amount which bears the same *ratio* to the *net income* of the taxpayer * * * as the average tax of representative corporations * * * bears to their average net income * * *", and in subsection (b) provides, "* * * the *ratios* between the average tax and the average net income * * * shall be determined by the Commissioner * * *". The essence of the statute is an average "*ratio*" derived from representative corporations to be applied to the net income which necessarily means the correct net income. It is a mere play upon words to say that the elements of discretion go to determining the tax. The inescapable fact is that the entire discretionary action of the Commissioner, namely, selection of representative corporations with all the elements entering into such selection, is confined to arriving at the *ratio*.

The court below did not review or set aside any discretionary act of the Commissioner, for it did not make any determination regarding abnormality, gross disproportion, or the selection of representative corporations. On the contrary, it only decided whether or not the taxpayer was entitled to certain additional deductions claimed by it and thus arrived at the correct net income, a function which the courts perform in practically every tax case presented to them. The court then applied to this correct net income the ratios which were determined by administrative action and which it had no authority to reject or change.

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[1] The term "special assessment" is not found in the statute but is a convenient though inexact term used to cover the steps taken under Sections 327 and 328.

To say that the court set aside any discretionary administrative action or performed any discretionary actions which are administrative is to ignore the facts of what happened below. There is no administrative discretion in the determination of net income for that is wholly a matter of law and arithmetic.

Federal Income and Profits Taxes Must Be Determined Upon the True Net Income.

It is a self-evident proposition that the income or profits taxes imposed by the revenue statutes are a percentage, rate, or ratio of the *true* net income of the taxpayer determined in accordance with the statutory definitions of gross income and deductions. Whatever the rates may be, and however they may be determined under the statute, they are to be applied to such true income and not to incorrect income. If the rates, whether they be stated in Section 230 (income tax rates) or in Sections 301, 302 and 328 (profits tax rates), are applied to incorrect income the result is incorrect taxes. If the income is judicially corrected, it must follow that a correction in the taxes results automatically.

The Extent of the Commissioner's Discretionary Powers Under Sections 327 and 328.

Under Section 327 the Commissioner must compute the ratio or rate from representative corporations:

(a) If he is unable to determine the invested capital as provided by the statute (see subdivision (a));

(b) In the case of all foreign corporations (see subdivision (b));

(c) Where the property paid in for stock was a mixed aggregate of tangibles and intangibles and the necessary segregations cannot be made (see subdivision (c));

> (d) Where on application by the taxpayer he finds that there is an abnormality of capital or income and the effect of such abnormality is to produce a tax which, when computed in the ordinary way, is grossly disproportionate to the tax when computed under Section 328 (see subdivision (d)).

The Commissioner acts in a discretionary capacity only under subdivision (d) where he alone is empowered to decide whether or not an abnormality exists and if so whether or not a gross disproportion in tax exists.[2] When he has made this decision he then must turn to Section 328 and find the ratio there described just as he must do in the cases under (a), (b) and (c).

Under Section 328 only the Commissioner can select "representative corporations whose invested capital can be satisfactorily determined * * * and which are, as nearly as may be, similarly circumstanced with respect to gross income, net income, profits per unit of business transacted, and capital employed, the amount and rate of war profits or excess profits, and all other relevant facts and circumstances". When he has made his selection it cannot be disturbed, in the absence of an abuse of his discretionary powers.[3]

There is nothing in either of these sections of the statute which says, as petitioners contend, that once he determines

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[2] *Williamsport Wire Rope Co.* v. *United States*, 277 U. S. 551, *supra*; *Duquesne Steel Foundry Co.* v. *Commissioner*, 41 Fed. (2nd) 995 (C. C. A. 3rd), affirmed *per curiam*, 283 U. S. 299; *Enameled Metals Co.* v. *Commissioner*, 42 Fed. (2nd) 213 (C. C. A. 3rd), affirmed *per curiam*, 283 U. S. 799; *Standard Rice Co.* v. *Commissioner*, 41 Fed. (2nd) 481 (C. C. A. 5th); *Cramer & King* v. *Commissioner*, 41 Fed. (2nd) 24 (C. C. A. 3rd); *Kekaha Sugar Co.* v. *Burnet*, 50 Fed. (2nd) 322 (Ct. App. D. C.); *Railway Supply Co.* v. *Burnet*, 51 Fed. (2nd) 437 (Ct. App. D. C.).

[3] *Brown's "Shamrock" Linens, Ltd.* v. *Bowers*, 48 Fed. (2nd) 103 (C. C. A. 2nd), cert. denied 283 U. S. 865; *Chicago Frog & Switch Co.* v. *United States*, 67 Ct. Cls. 662.

a net income no court can change it for the purpose of computing a profits tax or that once he computes a tax on the net income as determined by him no court can change that tax through the medium of changing income.[4] All of the decisions by the courts involving Sections 327 and 328 have been confined to whether the courts could *require* the Commissioner to allow special assessment under Section 327(d) (See authorities, footnote (2), page 9, *ante*); or whether the *rates* determined by the Commissioner under Section 328 through comparison with representative corporations could be judicially reviewed. (See authorities, footnote (3), p. 9, *ante*.)

In connection with the action taken by the Commissioner under Section 328, that is, the propriety of rates found by him from representative corporations, only two cases have gone to the courts. They indicate quite clearly that the discretionary action lies in the finding of the ratios or rates. In *Brown's "Shamrock" Linens, Ltd.* v. *Bowers, supra,* the Circuit Court of Appeals for the Second Circuit, in describing the question presented, said:

> "Thus it is apparent that the complaint attacks the correctness of the *ratio* used by the Commissioner and asks the court to review all the comparative data which under the statute must enter into his determination of such *ratio*." (Italics ours.)

In *Chicago Frog & Switch Co.* v. *United States*, 67 Ct. Cls. 662, the taxpayer complained of the selection of comparatives and the court's description of the taxpayer's contention is:

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[4] *Tax* equals *rate* times *income*. The rate, whether determined under Section 328 or found in the statute elsewhere, cannot be changed by any court. But the income may validly be corrected and the result must be a correction of the tax. If either of two factors is corrected a correction in their product follows.

> "* * * that said profits tax was not the amount which bore the same *ratio* to the net income of plaintiff * * * as the average tax of representative corporations * * * bore to their average net income * * *." (Italics ours.)

In *United States* v. *Henry Prentiss & Co., Inc.*, decided this term, the Supreme Court had occasion to consider Sections 327 and 328 in connection with a question different from that here involved. But the court characterized Section 328 in the following language:

> "Section 328 provides in effect that in cases covered thereby the tax shall be computed without reference to the value of the invested capital and shall be determined by the *ratio which the average tax of representative corporations engaged in a like or similar trade or business bears to their average net income.*" (Italics ours.)

Thus it is apparent that the Commissioner does not turn to representative corporations and select a profits tax from them. He selects the average ratio or rate from them and with such rate computes the profits tax by applying it to the net income.

The law, as pronounced in the cases just cited (p. 9, *ante*), is precisely the same law that the trial court applied in this case. In the pleadings the taxpayer objected to the comparatives that the Commissioner had used. The Government answered that such comparatives were not subject to judicial review. The point was argued, by agreement, in advance of trial and the trial court decided adversely to the taxpayer. The substance of the trial court's preliminary decision was reiterated in its final decision in the following language (R. 101, Nos. 476, 477):

> "The plaintiff, in addition to the amortization and depreciation claims in respect to the 1918 taxes, has sought a review of the commissioner's determination of its ex-

cess-profits tax rate for 1918. We feel that this court does not have jurisdiction to review the commissioner's ruling in this respect. See *Williamsport Wire Rope Co.* v. *United States,* 277 U. S. 551."

In correcting the net income for each year and applying the unreviewable rates to such income the court below neither reviewed nor set aside the Commissioner's discretionary acts. Its correction of the income was a matter of law and fact and its computation of the tax a mere matter of multiplication.

II.

The courts below could not do otherwise than apply to corrected net income the ratios determined by the Commissioner; and this was not prejudicial to the Government, for it gave the taxpayer a smaller judgment than it would have obtained under any other rates that could have been used.

The rates determined by the Commissioner are not reviewable. It is self-evident that profits taxes must be computed upon the true income. The result is that reached by the court below.

In an effort to avoid this legally correct and just result petitioners have resorted to sundry arguments, the sum and substance of which are that, if the Commissioner has determined a ratio under Section 328, the profits taxes which result from applying such ratio to an incorrect income may not be recovered. In other words, that under such circumstances no court can correct errors of net income however grievous. Carried to its ultimate conclusion petitioners'

argument means that the Commissioner may collect profits taxes in excess of the true net income or collect such taxes when there is no net income whatsoever. Such results could transpire without any abuse of discretion by the Commissioner for he might in perfectly good faith disallow a large deduction or include an item which constitutionally is not income[5] and proceed to compute the tax under Section 328 by fairly selecting comparative corporations on the basis of the net income determined by him. A court might, upon review, allow the deduction in question or strike out the disputed item from income, but be powerless to order a refund of any part of the erroneous profits tax.

If this court should reverse the judgment and deny recovery of any part of the profits taxes found by the Commissioner the result would be to approve a profits tax of $2,084,324.26 on a true net income of $3,291,410.30, or a profits tax rate of 63.33% instead of 54.54% for 1918. Similar action for 1919 would produce a profits tax rate of 19.10% instead of 18.31%. That action would be a real review and reversal of the Commissioner's discretionary action taken under Section 328 for it would set aside the rates which he found to be proper and substitute therefor higher rates—notwithstanding lower income.

The arguments resorted to by the petitioners in an effort to accomplish the foregoing results will not bear examination.

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[5] Practically every tax case that goes to the courts involves the propriety of deductions or income items. That the Commissioner has at various times sought to tax that which constitutionally is not income is well illustrated by a number of cases that have come to this court. (*Eisner* v. *Macomber*, 252 U. S. 189; *Miles* v. *Safe Deposit & Trust Co.*, 259 U. S. 247; *U. S.* v. *Supplee Biddle Hardware Co.*, 265 U. S. 189; *Edwards* v. *Cuba Railroad Co.*, 268 U. S. 628.)

Petitioners' Arguments Discussed.

Petitioners argue that if the court corrects the net income it cannot correct the profits tax without resorting to Section 301. This is a contradiction of all the other arguments because it implies that the court must reject the unreviewable rates adopted by the Commissioner and ignore the Commissioner's determination that there was an abnormality and gross disproportion which under the statute *requires* computation of the ratio under Section 328. Such action would clearly be a denial, and therefore a judicial review, of the Commissioner's discretionary action.

Their chief argument is that if the income is corrected the comparatives used by the Commissioner *may* no longer be representative within the meaning of Section 328 and that if the Commissioner were to make another selection he *might* choose comparatives which would show rates so much higher than 54.54% and 18.31% that the profits tax based upon the correct net income would be at least as high as that previously computed upon the incorrect net income. And further, they say, this might remove the gross disproportion mentioned in Section 327(d).

It is not said, even by way of argument, that the comparatives *would certainly* or *probably* cease to be appropriate for the corrected net income or that the Commissioner *would certainly* or *probably* select different comparatives if given the opportunity. As the court below well said:

> "It is a bare possibility that the reduction of the income to the proper and just amount might have some conceivable effect on the selection of representative corporations."

When this case was tried petitioners successfully objected to any evidence regarding the accuracy of rates under any con-

ditions. The accuracy of these rates became the law of this case. The courts are not required, and it is submitted are not at liberty, to speculate or surmise as to things that might or might not happen. Their function is to consider the record as they find it together with matters of which they may take judicial notice. Such bare possibilities do not justify a reversal of the judgment in this case.

The argument that correction of net income *might* move the Commissioner to use different comparatives and different rates is mere speculation. It is equally true that the corrections might *not* be sufficiently substantial to move the Commissioner to make any change at all. Courts are interested in facts rather than mere possibilities. If in truth the income corrections would have the effect which the Government asserts they *might* have, the burden was on the Government to prove it by evidence. For in the absence of evidence the presumption is that the Commissioner's comparatives and rates were correct.

Granting the possibility that a change in income might have some effect on the selection of representative corporations, it is quite apparent that if new comparatives were selected on account of the correction of income to a smaller amount the average ratio of tax to net income could under no circumstances be higher than the ratios found by the Commissioner; on the contrary such new ratios would be lower.

As already demonstrated it is fundamental that the profits tax bears a relation to net income, so much so that if the income is increased the *rate* increases; and if the income is decreased the *rate* decreases. Thus, with changes in income, the resulting tax changes are in a geometric proportion rather than in a mere arithmetic proportion. Therefore,

when the income is corrected downward there is a compelling conclusion that the tax must be reduced. Now if the Commissioner were to select new comparatives on account of the reduction of the taxpayer's income he would find that the reduction of income has not changed the capital employed[6] in the business and the gross income has not been changed. (The court changed net income by allowing deductions, leaving gross income undisturbed). He would then find a smaller net income which would mean smaller "profits per unit of business transacted" and smaller "amount and rate of war profits or excess profits." Therefore, his new comparatives should be similar to his old comparatives with respect to capital and gross income but should show lower net income, profits per unit of business, and excess or war profits. The average ratio of new comparatives with unchanged capital and gross income, but reduced net income (with attendant reductions in the other statutory elements) would inevitably be lower than 54.54% and 18.31%.

To support their assertion that this *might* not be true petitioners employ an illustration, set forth in Appendix "C" of their brief, showing a theoretical computation by special assessment before income is reduced and another theoretical computation with new comparatives after income is reduced. The fallacy of their illustrations lies in the fact

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[6] Section 328 provides that in selecting comparatives consideration is to be given to "capital employed". Obviously in abnormal cases this phrase does not mean statutory invested capital under Section 326 because such capital is not to be used under Section 328. The capital actually employed in business in an abnormal case includes capital assets that are valuable but which may not be included in "invested capital". That is an abnormal case, and when comparatives are selected the Commissioner is not to turn to those having a statutory invested capital similar to that of the taxpayer but to those having a statutory invested capital similar to the "capital employed" in the taxpayer's business.

that the average invested capital of the new comparatives is only 40% as great as the average invested capital of their old comparatives. In no other way could petitioners, by any computation made under the statute, show higher rates for a reduced income. In Appendix "B", page 24, *infra*, petitioners' illustrations are discussed and other illustrations are given which show that if new comparatives are used with the same or approximately the same capital but income reduced to the same extent that the taxpayer's income is reduced the result is profit tax rates *lower* than those determined for the incorrect, greater income.

Petitioners argue that if income is changed the use of new comparatives might result in no disproportion. In the first place, if no disproportion exists between the taxes recomputed under Section 301 and the taxes resulting from the use of the rates found by the Commissioner the Government is not harmed because as long as it receives the correct amount of profits tax the manner of computation becomes wholly immaterial. In any event, in the case at bar, the difference between the profits taxes under the court's judgment and as recomputed by the Bureau of Internal Revenue under Section 301 and set forth in their brief is great, being more than $100,000 for 1918 and more than $220,000 for 1919[7].

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[7]

	Section 301	*Court's Judgment*	*Difference*
1918	$2,197,633.50	$1,795,307.70	$402,325.80
1919	699,665.10	476,724.84	222,940.26

It would hardly require administrative discretion to say that the above differences constitute gross disproportions and a real hardship. Now if there could be a new selection of comparatives the average ratios would be lower, because of the reduced income, with the result that the above differences would be even greater.

Under no theory of this case can it be said that the judgment below establishes a profits tax that is improper because too low; on the contrary, the conclusion that a recomputation under Section 328 based upon the corrected net income should result in profits taxes even lower than those found by the court is irresistible. We concede the court had no power, however, to give judgment for any less profits taxes than it has done. But certainly the fact that the relief given is probably inadequate and legally cannot be made adequate is not justification for reversing the judgment and denying all relief.

Petitioners have cited the decision of the District Court for the Northern District of Ohio in *Cleveland Automobile Co.* v. *United States,* decided February 24, 1932. The court decided that the income as determined by the Commissioner was correct; therefore, everything it said with respect to the power of the courts to correct the profits tax if the income is corrected was dictum and unnecessary to the decision in the case. This decision is referred to and discussed at greater length at page 7 of our brief in opposition to petition for certiorari.

Another argument which petitioners urge is that this taxpayer applied for special assessment and when it was granted by the Commissioner the taxpayer was compelled to accept the result. In this connection petitioners point to the letter of December 23, 1925 (R. 75, Nos. 476, 477) in which the Assistant to the Commissioner said:

> "Before consideration can be given your application for special relief there must be a final determination of your tax liability computed on the basis of statutory invested capital."

The letter also provided that a protest might be filed and it is suggested that such may not have been done by the respondent. On page 17 of petitioner's brief appears the statement that it is customary to request acquiescence by a taxpayer in the amount of income and invested capital, "as was done in this case". The only authority for that statement is the language quoted above from the letter dated December 23, 1925. In point of fact the income tentatively determined by the Commissioner in that letter was changed in the letters of March 19, 1927, and July 11, 1927, which specifically refer to respondent's protests and oral conferences (R. 60, 70, Nos. 476, 477). This assertion of fact is unjustified.

The final determination of net income which quite clearly must be made before any tax can be computed by the Commissioner is his determination, and may be right or wrong. Invariably he makes his determination in every tax case regardless of the manner in which the tax may be computed. The statute imposes that duty upon him, but no taxpayer is required to accept his determination as final. [8]

The regulations contain no provision that a taxpayer applying for special assessment must agree with the Commis-

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[8] It would appear that in some special assessment cases the taxpayer and the Commissioner in fact formally agreed upon the net income before computation of the profits tax by special assessment. Compare *Commissioner* v. *Ohio Falls Dye & Finishing Works*, 50 Fed. (2nd) 660; *Norton Co.* v. *Commissioner*, 50 Fed. (2nd) 664. But there is nothing to indicate that any such agreement existed in the case at bar. In fact the entire history of the controversy conclusively refutes any such idea. The chief basis of this litigation was the act of the Commissioner in reducing the amortization allowance from $1,344,000, as determined by the Amortization Section in 1921, to the relatively small sum of $387,000 (R. 3, Nos. 476, 477), and the disallowance of depreciation taken in the returns and charged off on the taxpayer's books by the sum of $439,000 (R. 3, Nos. 476, 477). These large deductions were never acceptable to the taxpayer and were never agreed to by it.

sioner's determination. As a matter of fact in the majority of cases the application for special assessment was made at the time the return was filed,[9] as this taxpayer did for the year 1918 (Ex. LL, B. E. Vol. II, p. 635). It was customary also to entertain and allow applications for special assessment made after returns were filed, as was done in this case for the year 1919.

Once an application for special assessment has been filed and the Commissioner finds an abnormality and disproportion he must then compute the tax under Section 328. It is hardly conceivable that these *relief provisions* were designed as traps into which taxpayers might step and find themselves beyond hope of any judicial review of income and deductions that the Commissioner may determine. Such an argument, if applicable in a case of this kind, would likewise apply to all other special assessment cases where the taxpayers had no option but must have their taxes computed under Section 328 (see p. 8, *ante*).

When Congress enacted these sections of the law it did so with a report of the Senate Finance Committee before it to the effect that no part of Title III of the statute was more important; that the computation of profits taxes in the ordinary way would work great hardship in exceptional cases; and that the statutory method placed a heavy penalty on conservative financing and a premium on over-capitalization.

The report concludes with the following words:

> "Indeed without such classification the constitutionality of the whole tax might, because of its unequal

[9] Article 901, Regulations 45, provides that "a corporation which comes within the provisions of subdivision (d) of Section 327 may make application for assessment under the provisions of Section 328, which application shall be attached to its return in the form of a statement setting forth in full" certain information and data which is here unimportant.

operation, be open to serious question." (Senate Report No. 617, 65th Congress, Third Session, p. 14.)

Such language contradicts any thought that a taxpayer obtaining special assessment could be required to bargain away all right to judicial review of income and deductions.

CONCLUSION.

Petitioners' arguments all lead to the proposition that wherever a ratio of profits tax has been determined by the Commissioner under Section 328 the Commissioner's errors of income with the consequent errors in profits tax may not be corrected judicially.

It is respectfully submitted that such proposition is unsound legally as well as unjust, and that the decision of the court below applying the unreviewable rates to the correct net income should be affirmed.

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APPENDIX "A".

Section 301(a) and (b), Section 327, and Section 328(a) and (b) of the Revenue Act of 1918 are as follows:

"SEC. 301. (a) That in lieu of the tax imposed by Title II of the Revenue Act of 1917, but in addition to the other taxes imposed by this Act, there shall be levied, collected, and paid for the taxable year 1918 upon the net income of every corporation a tax equal to the sum of the following:

FIRST BRACKET.

"30 per centum of the amount of the net income in excess of the excess-profits credit (determined under section 312) and not in excess of 20 per centum of the invested capital;

SECOND BRACKET.

"65 per centum of the amount of the net income in excess of 20 per centum of the invested capital;

THIRD BRACKET.

"The sum, if any, by which 80 per centum of the amount of the net income in excess of the war-profits credit (determined under section 311) exceeds the amount of the tax computed under the first and second brackets.

"(b) For the taxable year 1919 and each taxable year thereafter there shall be levied, collected, and paid upon the net income of every corporation (except corporations taxable under subdivision (c) of this section) a tax equal to the sum of the following:

FIRST BRACKET.

"20 per centum of the amount of the net income in excess of the excess-profits credit (determined under section 312) and not in excess of 20 per centum of the invested capital;

SECOND BRACKET.

"40 per centum of the amount of the net income in excess of 20 per centum of the invested capital."

"SEC. 327. That in the following cases the tax shall be determined as provided in section 328:

"(a) Where the Commissioner is unable to determine the invested capital as provided in section 326;

"(b) In the case of a foreign corporation;

"(c) Where a mixed aggregate of tangible property and intangible property has been paid for in stock or for stock and bonds and the Commissioner is unable satisfactorily to determine the respective values of the several classes of property at the time of payment, or to distinguish the classes of property paid in for stock and for bonds, respectively;

"(d) Where upon application by the corporation the Commissioner finds and so declares of record that the tax is determined without benefit of this section would, owing to abnormal conditions affecting the capital or income of the corporation, work upon the corporation an exceptional hardship evidenced by gross disproportion between the tax computed without benefit of this section and the tax computed by reference to the representative corporations specified in section 328. This subdivision shall not apply in any case (1) in which the tax (computed without benefit of this section) is high merely because the corporation earned within the taxable year a high rate of profit upon a normal invested capital, nor (2) in which 50 per centum or more of the gross income of the corporation for the taxable year (computed under section 233 of Title II) consists of gains, profits, commissions, or other income, derived on a cost-plus basis from a Government contract or contracts made between April 6, 1917, and November 11, 1918, both dates inclusive."

"SEC. 328. (a) In the cases specified in section 327 the tax shall be the amount which bears the *same ratio* to the *net income* of the taxpayer (in excess of the

specific exemption of $3,000 for the taxable year, as the average tax of representative corporations engaged in a like or similar trade or business, bears to their average net income (in excess of the specific exemption of $3,000) for such year. In the case of a foreign corporation the tax shall be computed without deducting the specific exemption of $3,000 either for the taxpayer or the representative corporations.

"In computing the tax under this section the Commissioner shall compare the taxpayer only with representative corporations whose invested capital can be satisfactorily determine under section 326 and which are, as nearly as may be, similarly circumstanced with respect to gross income, net income, profits per unit of business transacted and capital employed, the amount and rate of war profits or excess profits, and all other relevant facts and circumstances.

"(b) For the purposes of subdivision (a) the *ratios* between the average tax and the average net income of representative corporations shall be determined by the Commissioner in accordance with regulations prescribed by him with the approval of the Secretary.

"In cases in which the tax is to be computed under this section, if the tax as computed without the benefit of this section is less than 50 per centum of the net income of the taxpayer, the installments shall in the first instance be computed upon the basis of such tax; but if the tax so computed is 50 per centum or more of the net income, the installments shall in the first instance be computed upon the basis of a tax equal to 50 per centum of the net income. In any case, the actual ratio when ascertained shall be used in determining the correct amount of the tax. If the correct amount of the tax when determined exceeds 50 per centum of the net income, any excess of the correct installments over the amounts actually paid shall on notice and demand be paid together with interest at the rate of ½ of 1 per centum per month on such excess from the time the installment was due."

APPENDIX "B".

Petitioners have argued that if the Commissioner were to select new comparatives to meet the condition of corrected income he *might* select comparatives as illustrated in Appendix "C" attached to their brief (p. 41). That illustration assumes a taxpayer's income and statutory invested capital (not "capital employed" in the business) as found by the Commissioner and then assumes comparatives with average invested capital of $300,000 and average net income of $100,000, the same as that of the taxpayer. The rate or ratio of profits tax resulting is 53.6%. Then follows a recomputation with new comparatives. The new comparatives show an average invested capital of only $120,000 with the result that there is a tax of $54,400, that is, a ratio of tax to income of 65.5%.

The fallacy of the illustration lies in the fact that the new comparatives have invested capital of only 40% of the previous comparatives, notwithstanding the fact that the taxpayer's capital employed in its business cannot possibly have been changed by reason of a correction downward of its income.

What the Commissioner should undoubtedly do if he were to select new comparatives would be to use representative corporations having substantially the same invested capital as the invested capital of that previously used but having smaller incomes. If this were done he would have the following:

New Comparatives with the same invested capital.

Average invested capital	$300,000
Average income	83,000
Average profits tax under Section 301 ..	40,000
Ratio of profits tax to income	48.31%

(Compare this with the rate of 53.6% established by the previous comparatives.)

Suppose the Commissioner in selecting new comparatives should seek an invested capital which is as much lower than that of the prior comparatives as the corrected income is lower than that of the income as determined by him, and this should certainly be the limit to which he might go. We would then have the following:

Average invested capital	$250,000
Average income	83,000
Average profits tax under Section 301 ..	44,000
Ratio of profits tax to income	53.01%

Here again the rate is below that previously established by special assessment, namely, 53.6%, and far below the 65.5% in petitioner's second computation by special assessment.

In his illustration, therefore, the Commissioner could not by new comparatives establish a rate as high as that previously found by special assessment except through the obviously incorrect expedient of reducing average invested capital to a greater extent than income is reduced. If in the case at bar he should select new comparatives under Section 328 after correction of the income by the court he could not establish rates as high as 54.54% and 18.31% without doing the same thing.

SUPREME COURT OF THE UNITED STATES.

Nos. 476, 477, 478.—October Term, 1932.

D. B. Heiner, Collector of Internal Revenue, Petitioner, 476 *vs.* Diamond Alkali Company.	On Writs of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.
D. B. Heiner, Collector of Internal Revenue, Petitioner, 477 *vs.* Diamond Alkali Company.	
C. G. Lewellyn, formerly Collector of Internal Revenue, Petitioner, 478 *vs.* Diamond Alkali Company.	

[March 13, 1933.]

Mr. Justice Roberts delivered the opinion of the Court.

These cases present the question whether, where the Commissioner of Internal Revenue has granted special assessments of profits taxes pursuant to § 328 of the Revenue Act of 1918 (40 Stat. 1093), a court, in an action for a refund, may recalculate the taxpayer's net income and recompute the tax by applying to the corrected net income the rate per cent. used by the Commissioner in his computation of the tax.

The Alkali Company filed returns for income and profits taxes for 1918 and 1919 and paid the tax shown to be due. The Commissioner proposed certain changes in income and capital as reported, principally due to decreases in amortization and depreciation allowances. At some date not disclosed by the record the company asked that its profits taxes be computed pursuant to Sections 327 and 328 of the act. The request was denied and correspondence and conferences ensued between the Commissioner

and the taxpayer in an effort to settle the disputed items. The demand for computation of the taxes pursuant to the special assessment sections was pressed by the company. Twice during the period of negotiation the Commissioner advised that until the true net income was ascertained the propriety of special assessment could not be determined. Finally, in July, 1927, as a result of audits and investigations, he found the company's net income, and decided that, owing to abnormal conditions affecting its capital or income, assessment according to the usual method under Section 301 would work an exceptional hardship, and relief should be granted pursuant to Sections 327 and 328. He so notified the respondent, enclosing a calculation of the taxes made by him pursuant to Section 328. The taxpayer protested on several grounds, amongst others, that the net income as determined under Section 301 was excessive, and that the ratio of tax to net income obtained by the Commissioner by comparison with the taxes of other representative corporations, as provided in Section 328, was too high. It did not, however, as was its right, appeal to the Board of Tax Appeals from the determination of net income.

In November, 1927, the Commissioner made an assessment in accordance with his findings and demanded payment of a deficiency thereby disclosed. The respondent paid under protest and filed claims for refund, asserting the same objections it had previously urged. The claims were rejected and the respondent brought suits to recover the alleged overpayments. The District Court found that additional amounts should have been allowed for amortization, reduced the net income as determined, thereupon recomputed the taxes on the reduced income by applying the rate per cent. used by the Commissioner in his computation, and rendered judgment in favor of the respondent. Both parties appealed. The Circuit Court of Appeals increased the amortization allowance, made additional deductions from gross income for depreciation, found a net income much less than that fixed by the District Court, and held that the tax should be recomputed by applying the rate used by the Commissioner to the new figure found as the net income.

Section 327 (d), so far as here material, enacts that "Where upon application by the corporation the Commissioner finds and so declares of record that the tax if determined without benefit of this section would, owing to abnormal conditions affecting the

capital or income of the corporation, work upon the corporation an exceptional hardship evidenced by gross disproportion between the tax computed without benefit of this section and the tax computed by reference to the representative corporations specified in section 328", the tax shall be computed as provided in the latter section. Section 328 declares that the tax shall be "the amount which bears the same ratio to the net income of the taxpayer" as the average tax of representative corporations engaged in a like or similar trade or business bears to their average net income, and directs that in computing the tax the Commissioner shall compare the taxpayer only with representative corporations whose invested capital can be satisfactorily determined in accordance with section 326, which are as nearly as may be "similarly circumstanced with respect to gross income, net income, profits per unit of business transacted and capital employed, the amount and rate of war profits or excess profits, and all other relevant facts and circumstances."

In *Williamsport Wire Rope Co.* v. *United States*, 277 U. S. 551, it was decided that the allowance of special assessment is a matter of administrative discretion; and it was further said that the selection for comparison of representative corporations engaged in a like or similar trade or business is also a question of discretion. The Commissioner cannot make an administrative finding upon the question for decision under Section 327 (d) or that under 328 until he has determined the net income of the taxpayer. See *United States* v. *Henry Prentiss & Co. Inc.*, No. 234, October Term, 1932, decided January 9, 1933. He must compare the income of the taxpayer with that of corporations he deems representative in order to determine abnormality or gross disproportion between capital and income. When he comes to compute the ratio or rate of tax to be applied to the taxpayer's net income, as prescribed in Section 328, he obviously will consider as a factor the ratio of tax to net income of the same representative corporations he examined for the purpose of deciding whether he should grant special assessment under Section 327 (d).

The parties are in agreement that the *Williamsport Wire Rope Co.* case, *supra*, precludes revision, correction, or abrogation of the Commissioner's administrative discretionary findings, where, as here, there is no allegation of fraud. On the one hand the petitioners claim that the decisions below amount to such abrogation and the making of a new finding as to the right of special assess-

ment and a fresh computation of the tax upon revised net income; on the other, the respondent says that the courts recognized the binding character of the Commissioner's findings, enforced rather than set aside his allowance of relief, and adopting the rate found by him, applied it to the true statutory net income as judicially determined in accordance with law.

We think the petitioners' position is correct. The taxpayer's true net income was an essential factor in the problem. Until that was known the Commissioner could make no proper or satisfactory comparison with conditions prevailing in other corporations similarly circumstanced. We cannot say that if the income had been substantially less than the figure he used he would have granted special assessment under Section 327 (d). Moreover, with a different net income, he might well have had to compare the relevant conditions in respondent's business with the operating results of corporations other than those he selected on the basis of respondent's net income as found, and might have concluded that a different ratio of tax to net income was applicable in respondent's case.

The grant of special assessment and the ascertainment of the rate or ratio of tax to be applied to the net income of the taxpayer are indissolubly connected by the terms of the statute. The exercise of the discretion in both aspects is committed to the Commissioner and to the Board of Tax Appeals upon review of his action. That discretion cannot be reviewed by the courts, nor exercised by them in place of the administrative officer designated by law. It is beyond the power of a court to usurp the Commissioner's function of finding that special assessment should be accorded, and equally so to substitute its discretion for his as to the factors to be used in computing the tax. The courts below were in error in adopting the rate chosen by the Commissioner and applying it to a net income other than that which he used in making his comparisons and arriving at the rate. The respondent's tax could only be computed in accordance with Section 301 or under Section 328. The former prescribes the elements to be considered, and error in the computation remains subject to judicial correction; the latter grants the taxpayer the benefit of discretionary action by the Commissioner, and precludes judicial revision or alteration of the computation of the tax.

The judgments must be reversed and the cases remanded for further proceedings in conformity with this opinion.

Reversed.